Ministry of Foreign Affairs of the Netherlands

IOB Evaluation

In search of focus and effectiveness

Policy review of Dutch support for private sector development 2005-2012 (extensive summary)

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Policy review of Dutch support for private sector development 2005-2012 (extensive summary)[1]

January 2014

[1] The basis for this extensive summary is a report that was published in Dutch under the title '*Op zoek naar focus en effectiviteit. Beleidsdoorlichting van de Nederlandse inzet voor private sector ontwikkeling 2005-2012*'. The Hague, January 2014. IOB Evaluation no. 389. This summary devotes less attention to the analysis of the Dutch set of policy instruments. The findings and issues for further consideration regarding Dutch policy are almost fully rendered.

Preface

Private sector development (PSD) is a central focus of the current development cooperation policy. By strengthening the entrepreneurial climate in developing countries, the policy aims to create better opportunities for private investment, increase employment opportunities and ultimately also reduce poverty. The government has actively committed itself to achieving these objectives and in its effort has mobilised the Dutch business sector.

This policy review of Dutch support for private sector development focuses on the relevance, effectiveness and coherence of the instruments and the contribution that the business sector has made to economic growth and poverty reduction in developing countries. The review describes and analyses the Netherlands Ministry of Foreign Affairs' policy and expenditures during the period 2005-2012. The review will play a part in establishing accountability for the implementation of the policy, but it also aims to create insights that can be used to formulate future policy.

Policy reviews make use of existing evaluations of the policy. This report's approach deviates slightly from that. The Policy and Operations Evaluation Department (IOB) has expanded on the evaluation approach by using conclusions from international literature because it appears there are only a handful of robust, high-quality evaluations of Dutch PSD programmes. The review follows the same categorisation of five clusters (in effect, outcome areas) used by the Ministry of Foreign Affairs: (1) infrastructure, (2) financial sector development, (3) market development, (4) knowledge and skills and (5) laws and regulations. The review also focuses special attention on public-private partnerships (PPPs) and the role that international corporate social responsibility (ICSR) plays in PSD policy. By way of four country case studies, the policy review examines the question of coherence in the set of PSD instruments.

Dutch support has generated visible outputs in many areas. Nonetheless, we are not any closer to achieving our ultimate development objectives, nor is there as prominent a focus on poverty as there should be. The effectiveness of the PSD instrument is limited by the fact that specialised programmes devote particular attention to a number of specific problems, while in practice there are actually multiple – interrelated – bottlenecks. Moreover, IOB is critical of the appraisal that activities are completely additional to the market and would not have occurred without public assistance. Coordination between programmes and alignment with local needs do not always take place, partly because three quarters of the PSD programmes are managed from the Netherlands.

The policy review was conducted under the supervision of IOB evaluators Max Timmerman, Antonie de Kemp and Jan Klugkist, with the support of research assistants Jiska Gietema (until March 2013) and Bart Woelders. Internal commentary was provided by Peter Henk Eshuis, Paul de Nooijer and Frans van der Wel. The external reference group consisted of the following people: Renko Campen (independent consultant, ex-chairman of the executive board at DHV), Rob van Tulder (professor of international business-society management at the Rotterdam School of Management at Erasmus University), Robert-Jan Scheer (strategic advisor at DDE, the Sustainable Economic Development Department of the Ministry of Foreign Affairs) and Thijs Woudstra (DIO, the International Enterprise Department – Directorate-General for Foreign Economic Relations). The field studies conducted in Bangladesh, Ethiopia, Burundi and Vietnam were supervised by Sönke Buschmann (Triodos Facet).

IOB would like to thank all those involved in this policy review for the information and critical feedback that they have provided.

IOB assumes final responsibility for this report.

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List of abbreviations

ADB	Asian Development Bank
AfT	Aid for Trade
AIV	Advisory Council on International Affairs (*Adviesraad Internationale Vraagstukken*)
BRICs	Brazil, Russia, India and China
CBI	Centre for the Promotion of Imports from Developing Countries (*Centrum tot Bevordering van de Import uit ontwikkelingslanden*)
CSR	Corporate social responsibility
DANIDA	Danish International Development Agency
DC	Development cooperation
DDE	Sustainable Economic Development Department of the Ministry of Foreign Affairs (*Directie Duurzame Economische ontwikkeling*)
DFID	Department for International Development (United Kingdom)
DGIS	Directorate-General for International Cooperation of the Ministry of Foreign Affairs (*Directoraat-Generaal voor Internationale Samenwerking*)
ECP	Expert coaching programme
EU	European Union
FDI	Foreign direct investment
FIRST	Financial Sector Reform and Strengthening Initiative
FMO	Dutch Development Finance Institution (*Financieringsmaatschappij Ontwikkelingslanden*)
FOM-OS	Fund Emerging Markets (*Fonds Opkomende Markten – Ontwikkelingssamenwerking*)
FTE	Full-time equivalent
GDP	Gross domestic product
GNP	Gross national product
GPFI	Global Partnership for Financial Inclusion
GTFP	Global Trade Finance Program
IBRD	International Bank for Reconstruction and Development
ICF	Investment Climate Facility for Africa
ICSR	International corporate social responsibility
ICT	Information and communication technology
ICTSD	International Center for Trade and Sustainable Development
IDF	Infrastructure Development Fund
IDH	Sustainable Trade Initiative (*Initiatief Duurzame Handel*)
IEG	Independent Evaluation Group
IFAD	International Fund for Agricultural Development
IFC	International Finance Corporation
IFDC	International Fertilizer Development Center
IMF	International Monetary Fund
INRA	National Institute for Agrarian Reform, Bolivia (*Instituto Nacional de Reforma Agraria*)

IOB	Policy and Operations Evaluation Department of the Netherlands Ministry of Foreign Affairs (*Inspectie Ontwikkelingssamenwerking en Beleidsevaluatie*)
KfW	German Reconstruction Credit Institute (*Kreditanstalt für Wiederaufbau*)
LDCs	Least-developed countries
MASSIF	Micro And Small Enterprise Fund
MILIEV	Environmental and Economic Self-Sufficiency (*Milieu en Economische Verzelfstandiging*)
MMF	Matchmaking Facility for Developing Countries
NCSTE	National Center for Science and Technology Evaluation (China)
NGO	Non-governmental organisation
NIPP	Netherlands-IFC Partnership Program
ODA	Official development assistance
ODI	Overseas Development Institute
OECD	Organisation for Economic Co-operation and Development
OECD-DAC	OECD Development Assistance Committee
OPM	Oxford Policy Management
ORET	Development-related Export Transactions (*Ontwikkelingsrelevante Export Transacties*)
ORIO	Infrastructure Development Facility (*Ontwikkelingsrelevante Infrastructuurontwikkeling*)
PIDG	Private Infrastructure Development Group
PPP	Public-private partnership
PSI	Private sector investment programme
PSD	Private sector development
PSOM	Programme for Cooperation with Emerging Markets (*Programma Samenwerking Opkomende Markten*)
PUM	Netherlands Senior Experts Programme (*Programma Uitzending Managers*)
RPE	Ministerial decree on performance measurement and evaluation (*Regeling Periodiek Evaluatieonderzoek*)
SER	Social and Economic Council of the Netherlands (*Sociaal Economische Raad*)
SMEs	Small and medium enterprises
TCX	The Currency Exchange Fund
TK	Dutch House of Representatives (*Tweede Kamer der Staten-Generaal*)
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
US	United States
USAID	United States Agency for International Development
WRR	Dutch Scientific Council for Government Policy (*Wetenschappelijke Raad voor het Regeringsbeleid*)
WTO	World Trade Organization

Findings and issues for further consideration

The findings of the evaluation are modelled on the intervention logic and the RPE. The first finding concerns the relevance of Dutch support (ex ante): which problems did the Netherlands aim to solve with the available instruments? The second finding continues with the direct results (outputs). Finding three examines the effectiveness (outcome and impact) of the many different instruments. Findings four and five analyse the way in which the Netherlands used the instruments. In doing so, finding four mainly focuses on how purposeful the instrument has been, while finding five concerns the added value of the public instruments in addition to the private ones. The sixth finding deals with the coherence of the instruments, and the seventh does the same for their administration. In line with the findings, several issues for further consideration have been identified for Dutch policy.

1. *The ministry uses its PSD programmes to address important bottlenecks for the development of the private sector in developing countries.*

A comparison with the bottlenecks mentioned in international literature confirms the relevance of the specific clusters identified in Dutch policy. This is especially clear with the programmes that aim to strengthen infrastructure. In many developing countries, especially in Africa, there are serious shortcomings in this area. One billion people do not have access to passable roads, and another 300 million people do not have electricity. Safe drinking water and sanitation facilities are still out of reach for another 2.4 billion people. Moreover, the literature reveals that inadequate infrastructure is a major constraint to economic growth and poverty reduction. The lack of financial resources is huge, however. The estimated gap that will emerge between now and 2030 is EUR 43 billion. Investing in infrastructure rarely appeals to the private sector. This is especially the case for energy, transport (roads), and water and sanitation.

A number of major Dutch programmes address the above-mentioned bottlenecks, especially energy supplies and transport infrastructure. The ministry spent a total of more than EUR 1.2 billion on strengthening infrastructure between 2005 and 2012.

In addition, the Netherlands is trying to remove barriers to private sector development. Small and medium enterprises invariably cite poor access to financial services as one of the largest obstacles to growth. Small enterprises in particular face high interest rates and other financial barriers, such as high costs or a minimum charge to open a bank account. Dutch support between 2005 and 2012 amounted to almost EUR 740 million.

The ministry also supports organisations that focus on market development, often with the aim of improving market access for small producers (frequently in agriculture). Small enterprises have to contend with high transaction costs, market risks and limited information. Between 2005 and 2012, the ministry contributed EUR 550 million to programmes focused on this goal (16% of the PSD expenditure).

Other programmes use a host of different paths in an attempt to strengthen knowledge and technological skills in enterprises and promote technology transfer. The total amount for the period 2005-2012 amounts to EUR 615 million, approximately 18% of the total.[2] Although good evaluations are scarce on this point, there is quite a large consensus internationally that the lack of knowledge and skills and the poor access to technology present an obstacle to private sector development. The *World Development Report 2013* shows that many job opportunities in developing countries are concentrated in small businesses that are not particularly dynamic. Productivity is low, often due to a combination of insufficient skills and poor access to modern technology. The businesses create jobs, but they are just as easily lost again. Different Dutch programmes are trying to break this pattern.

Dutch expenditure in the area of laws and regulations is limited (less than 2% of the total). In part, this is because support in this area requires almost by definition far fewer financial resources than investing in infrastructure, for example. Moreover, the cluster is much less conducive to bilateral engagement and much more to an approach that uses multilateral channels. The Netherlands uses a few bilateral programmes to support land reform and the registration of land ownership. This could help to provide access to land and investments in land.

2. *The implementing organisations used the available resources to develop and finance a wide range of activities, which in most cases resulted in substantial outputs and considerable reach.*

The implementing organisations and evaluations reported mainly about achieving direct outputs, such as roads and power plants, but also about the size of loans to banks, for example. Following are several examples.

Infrastructure:

- A programme's support to encourage infrastructure projects (ORET) resulted in facilities for drinking water and sanitation (especially in Ghana), energy (in countries such as Madagascar, Tanzania, Ethiopia, Suriname and Indonesia), wet infrastructure (mainly dredging ports), health care (medical systems, in countries such as Tanzania, Zambia, Ghana, China and the Philippines) and transport (boats for countries such as Cuba, Colombia and Indonesia and buses for Ghana). According to the latest evaluations of this programme, 36 of the 50 examined projects actually managed to improve infrastructure.
- The fund for infrastructure projects in developing countries (FMO/IDF) had a portfolio of EUR 273 million in late 2012, which was used to financially support several dozen infrastructure projects, including energy (28%), immovable infrastructure (35%) and water (9%). By the end of 2012, 93% of the fund had gone to low-income countries, and the remaining 7% to lower middle-income countries.

Financial sector development:

- In 2012, 48% of the portfolio for financing SMEs (FMO/MASSIF), which amounted to more than EUR 300 million, was invested in financing SMEs and 27% was used for microcredit.

[2] This policy review is not taking into consideration support for vocational education.

That year, almost 59% of the resources were issued to low-income countries and another 45% to lower middle-income countries. Countries in Africa and Asia both had a share of approximately one third of the total.

Market development:

- The programme in support of export from developing countries (CBI) helps several hundred businesses annually. It does this mainly by strengthening business support organisations (71 times between 2005 and 2012), market information programmes (13), knowledge and skills transfer (63 projects) and the programme for export support (38 times). The latter programme generally supports 25-40 enterprises for each individual export coaching programme (ECP). All in all, CBI operates in 27 sectors and 48 countries, though in the period 2005-2011 almost half of the resources went to six countries (India, Colombia, Bolivia, Indonesia, Peru and South Africa).

Knowledge and skills:

- Every year, more than a hundred enterprises in about 50 countries develop activities with the support of a private sector investment programme (PSOM/PSI). It mainly concerns projects in agriculture and energy. On average, the enterprises create 81 jobs and train almost 100 people with a subsidy of EUR 500,000. According to the PSOM/PSI evaluation, 21 of the 32 examined projects contributed to the emergence of an economically healthy enterprise, job growth, innovation and knowledge transfer.

3. There is little information about achieving the ultimate objectives, including poverty reduction.

In order to determine the impact and the likelihood of achieving the ultimate objectives, it is not only important to set up a number of services (outputs) with Dutch resources, but in particular to gauge what their impact will be ultimately for entrepreneurs and households. To gain more insight into this, IOB examined 32 programmes in total. The ministry spent EUR 2.5 billion between 2005 and 2012 on these 32 programmes, which amounts to 75% of PSD expenditures. Of these 32 programmes, 30 were evaluated in one form or another.[3] On the other hand, only six programmes underwent an extensive evaluation for effectiveness.[4] Evaluations of another nine programmes did devote some attention to that, but not enough to draw robust conclusions about the impact of the programmes.

Evaluations often report on the reach or the implementation by immediate beneficiaries, but only rarely about the impact on the ultimate target groups, including specific consequences for women or the environment, for example. Only a few evaluations focused on the ultimate objectives in terms of improving incomes, reducing poverty and economic growth. When they did focus on these aspects, it was usually not based on systematic research. Notable exceptions in the area of PSD are the different impact evaluations on microfinance, which do devote attention to the impact on women. When detailed impact

[3] That could include a review.

[4] These figures incorporate both ORET evaluations from 2006. Strictly speaking, they are not being considered because they are not related to expenditures during the period 2005-2012. Therefore, 20% of all expenditures have been extensively evaluated.

studies were conducted, the impact was often more limited than previously estimated.[5] The causes include inadequate focus, particularly on poverty, an overly optimistic appraisal of the trickle-down effects, implementation problems and inaccurately estimated behavioural responses. It usually did not concern an isolated problem.

The IOB evaluation of the infrastructure fund for least-developed countries (FMO-IDF) concluded that a slight majority of the invested resources were additional to the high impact (51%); for the remaining resources, the expenditures were non-additional (37%) or the development impact was limited (12%).[6] Projects with a potentially high or actually high development impact mainly concerned water and sanitation and energy. IOB was more critical of the enclave-like investments in a titanium mine in Mozambique. The apparent benefits for the local population turned out to be unrealistic in this case. In several other IDF projects, FMO only took over existing financing schemes. These projects did not lead to new investments.

A review of the impact that programmes for SMEs had on employment opportunities concluded that although financing is important, it is also important that it focuses on target groups and their specific problems (Grimm, 2013). Indeed, such programmes are only effective when they are sufficiently demand-driven. According to an evaluation of FMO's SME portfolio, the instrument focuses too much on larger and well-known financing institutions and not on smaller, more specialised and less developed institutions for microfinance. The evaluation does not mention the impact of this. Impact evaluations of microcredit show that many of these programmes do not meet expectations. It is not so much the random provision of credit to households that contributes to economic growth, but more the improved access to finance for enterprises.

Evaluations of Dutch programmes that try to promote the integration of markets and increase knowledge and skills are generally highly process and output-oriented; they tell us little or nothing about the achieved effects, such as improved incomes and poverty reduction. When they do, it is not based on systematic research. A consultancy firm (Triodos Fact, 2009), for example, does indicate how many businesses used export support (CBI), but this does not necessarily mean that they would not have achieved some of these exports without this support. Scientific research on export programmes generally sees the promotion of export as having a lower level of impact. One concern with the programmes for strengthening knowledge and skills is that the kinds of expertise Dutch entrepreneurs have does not by definition dovetail with the information needs in recipient countries.

There is little empirical information on the effectiveness of public-private partnerships (PPPs) in PSD programmes. One reason for this is that evaluations often devote little attention to the specific role played by the form of cooperation. Often, the public partners

5 Similarly, the 'iron law' of Rossi (1987) argues that the better an evaluation's design is, the greater the chance that the researchers will not measure an impact.

6 Additionality refers to outputs that would not have been achieved in the market without the programme.

in PPPs are not permanently involved during implementation. Moreover, there are not always clear agreements about the distribution of risks and revenue. A systematic review, conducted on IOB's request, identified six factors that are important when involving PPPs, including a permanent role with clear guidelines for the government, a common vision, mutual trust and a balanced distribution of interests (IOB, 2013c).

An increasing number of businesses are also reporting on the use and impact of international corporate social responsibility (ICSR). There has been limited independent control of the claimed results, however. The outcomes of the various interventions are difficult to compare as well because a range of different indicators were used.

The lack of systematic evaluations in the area of private sector development is not a problem specific to the Netherlands. Various international researchers describe a lack of good evaluations in this area. In general, the quality of PSD evaluations lags behind those in the social sectors (such as education, health, and water and sanitation).

The following reasons have been cited for this lack of systematic evaluation:
- The development impact of PSD programmes are apparently difficult to measure;
- The different programmes and funds finance a (limited) part of the projects; and
- The programmes and funds finance highly heterogeneous activities.

There is no fundamental difference with the social sectors on these points. The most important reason for the limited number of impact evaluations in the area of PSD appears to be primarily because implementing organisations (and the ministry) have traditionally focused on financing and immediate outputs and much less on the development impact.

Partly on the initiative of IOB, the ministry made agreements with the administrators of the PSD programmes in 2012 to improve evaluations, for example by introducing an evaluation protocol and by making available tools for systematically measuring impact. It is still too early to report on the results, however.

4. *The implementation process of programmes managed centrally from The Hague often focused insufficiently on creating development relevance or achieving the objective of reducing poverty.*

While the Dutch PSD portfolio may have been relevant on paper, in practice the opportunities were not always fully taken advantage of. The policy review, for example, reveals that there is no link in any of the central programmes between the use of resources and the levels of income in recipient countries. A large part of the expenditures (subsidies) for the major programmes went to higher middle-income countries such as Suriname, the Maldives, Colombia, Jamaica, and Bosnia and Herzegovina. A significant part of the expenditures used to promote export (CBI) and technical assistance to companies (PUM) supported enterprises in similar countries. Companies and institutions in these countries are often in a much better position to bear consultancy costs themselves than comparable organisations in the poorest countries. Indeed, it raises the question of whether other instruments, such as concessional loans, are not more appropriate for supporting these (higher) middle-income countries. Conversely, the programme with the greatest focus on the poorest countries, namely the Infrastructure Development Fund, is precisely the one that works with loans and shares. Various evaluations reveal that programmes focused inadequately on poverty reduction and devoted too little attention to development relevance. This is not a specifically Dutch problem though. Evaluations by IEG (2008; 2011); White (2008); KfW (2010) and the Asian Development Bank (2012) reveal similar problems in areas such as electrification, roads and microfinance.

Different factors contribute to this limited development relevance. A first factor is that the agreements between the ministry and the implementing organisations do not focus on it sufficiently. Although this is the objective of the various agreements, it is barely incorporated into the conditions for financing. To achieve the anticipated impact, implementing organisations often use the information provided by applicants. A second factor is the ministry's limited guidance of the PSD organisations (see finding 7). An extensive budget or selection according to the order in which requests were received did not mean choices were made based on the anticipated impact either. The threat of underspending resulted in pressure to spend and supply management, and it reduced the need to reflect on the development relevance. This was especially the case when new programmes were launched, and the ministry and implementing organisation underestimated teething troubles.

Another reason why implementing organisations stopped focusing on the development relevance and poverty reduction is that several organisations had a dual objective. One was to increase the involvement of the business sector in development cooperation, in part by tying aid. The old, but still valid, Tinbergen rule states that the number of policy tools should be at least equal to the number of policy objectives. The reason for this is not only that objectives can conflict with each other, but also that each objective may require a completely different kind of implementation. That is the case here too. It concerns independent objectives, which only cross paths in specific cases. One can only speak of a confluence of interests if the Dutch business community is well equipped to solve specific development problems. But this is precisely what raises the question of whether tying aid is necessary. Tying aid entails the risk of sub-optimal allocation. The economic literature generally mentions a negative impact for recipient countries, including higher prices (15%-30%). In addition, tying aid limits the number of local providers one can use. It is far from evident that the best opportunities for Dutch businesses are in the poorest countries. Dutch exports to and investments in these countries are limited and, conversely, the Netherlands is rarely an important trade partner (with the exception of the import of raw materials from several countries). The absence of a relationship between development and expenditure mentioned above points to this potential conflict.[7] There is a risk that linking two completely different objectives will not create any synergy and only provide a sub-optimal solution: recipient countries will receive a service that it would not, a priori, have chosen itself, but at the same time the resources were also used in countries where the potential for growth for the Dutch business sector is limited.

7 This relationship does exist for PIDG, a multilateral initiative.

In practice, few companies actually benefit from the available instruments: between 2007 and 2012, half of the resources from the most comprehensive programme for infrastructure development (ORET) went to eight companies, who incidentally were not all Dutch companies. In that sense, this programme was not so much one for the (Dutch) business sector as it was a programme for a few major companies. The evaluation of this programme from 2006, and so from the previous period, concludes that the long-term impact for the Netherlands, in the sense that it strengthened trade relations and generated follow-up orders, was limited. Recent econometric research also suggests that the benefits of tying aid are very limited, if not absent, for the exporting countries.[8]

5. *Various programmes for private sector development assume too readily that the support is additional to the market. As a consequence, the impact is overestimated.*

The concepts of 'additionality' and 'catalytic impact' play a key role in PSD programmes. To begin with, funding must be additional to the market, which means that commercial parties are not prepared to finance a project on reasonable conditions because the risks are too high. The catalytic effect is the ability of funds to use the financing to generate other resources. If a public fund takes on the lion's share of the risk, then the project will appeal to commercial entrepreneurs again. The key advantage is that public resources can have a leverage effect, which makes it possible to start large-scale projects with relatively limited financing.

The policy review reveals that additionality is too readily assumed by implementing organisations. The fact that a government or (often) an entrepreneur seeks public financing too easily leads to the conclusion that they cannot secure private financing. Various evaluations show that implementing organisations do not sufficiently investigate to what extent available resources can actually remove obstacles. Evaluations of Dutch programmes cite examples of projects that were non-additional. Moreover, the demand for revolving funds can lead fund managers to focus on less risky projects, which the market already (partly) provides for. An example is the financing of telecommunications. Spending pressure can be another factor that leads people to not adhere strictly to the demand for additionality.

Programmes that are non-additional are not effective either: after all, it concerns an activity that would be undertaken anyway, with or without the contribution of a programme. The policy review reveals that the assessment of the effectiveness of the different programmes is therefore less positive as a result. The evaluation of an incentive programme for business investment (PSOM/PSI) is an example. According to the evaluation, 21 of the 32 examined projects were effective. A number of projects, however, were non-additional or only additional to a limited extent. The latter means that on balance the programme was effective in one out of three projects and ineffective in one out of eight. Almost half of the projects were somewhere in between.

8 IOB research on the impact of development aid on Dutch exports. Forthcoming.

Implementing organisations and consultants overestimate the catalytic impact in similar fashion. It turns out that in cases where the organisation cites extensive leverage effects (PIDG), there is financing by a conglomerate of funds and development banks, who all contribute to the positive effects.

There is always the danger of market distortion when programmes are non-additional. The risk is even higher when there is direct support from companies (PSOM/PSI) or when companies finance provisions (ORET). This element received little attention in the assessment ex ante as well as in the evaluation.

6. *The Netherlands supports specialised instruments that operate almost independently. There is little exchange between them. This does not contribute to effectiveness, because in many cases there is a more complex problem at work.*

The implementation of the Dutch PSD policy is characterised by a large number of separate specialised instruments, in which central implementing organisations are highly independent. The coordinating role of the ministry and embassies is limited, and the implementing organisations hardly ever actively seek cooperation for problems that they cannot address themselves. The fragmented use of instruments encourages an approach that focuses on the solution that the instrument offers rather than the problem itself.[9] It contributes to supply management, in which the central organisations want to serve the largest number of countries and partners as possible, and that, in turn, leads to further fragmentation. There is a lack of incentive to cooperate, which comes at the expense of effectiveness.

Approaches that focus on one problem are often less effective because different bottlenecks exist. They are often caused by a combination of factors, including inadequate physical infrastructure, insufficient access to capital and deficient knowledge and skills. The potential impact often depends on the extent to which the national climate for entrepreneurship leaves room for individual businesses and sectors to operate. For example, despite the difficulty that poor households and small businesses have in accessing credit, support from local banks is often lacking. It is therefore important to combine the financial instruments with interventions that solve other bottlenecks.

An analysis of the distribution of spending by five major programmes in different countries reveals that the current list of countries could be limited without much objection because the lion's share of the spending goes to a limited number of countries.[10] Between 2007 and 2012, more than 40% of an infrastructure programme's resources (ORET) went to activities in three countries: Ghana, Tanzania and China. The expenditures were also very unevenly distributed with other major central programmes. This raises the question of whether the

[9] The British development organisation DFID uses an alternative approach, in which the starting point is not the instruments but the problem. This encourages a more holistic approach.

[10] This analysis comprises ORET, PSOM/PSI, CBI, PUM and three government funds managed by FMO (MASSIF, IDF and the CD programme). IOB has therefore incorporated the three FMO funds as one in its analysis, which covers the period 2005-2011.

Netherlands can increase the efficiency of aid by limiting the list of countries, as was the case with bilateral aid. It is easier to achieve coordination and synergy in such cases.

7. *There are a limited number of available (specialised) staff members at the ministry who can offer guidance to the PSD programmes. There has been little effort to create accountability for outsourcing to independent PSD organisations or awarding subsidies.*

Approximately 230 employees at the major implementing organisations in the Netherlands work on implementing the programmes, while the ministry has 17 employees who are directly involved in managing the programmes in the five PSD policy clusters. As a result, the ministry sometimes had difficulty finding sufficiently qualified policy advisors. The limited number of available FTEs, fluctuating levels of expertise and frequent transfers all played into the hand of seriously inadequate supervision.

Issue for further consideration

Based on the findings in this policy review, and in light of recent developments, IOB has identified a number of issues for further consideration for the design of Dutch PSD policy.

1. *Transparency about objectives and instruments in relation to the level of development in recipient countries*

From 2010 onwards, PSD policy has defined development relevance and poverty reduction, as well as the contribution to the Dutch economy, as incentives for Dutch state support. The 'new agenda for aid, trade and investment' aims to further integrate Dutch economic interests and support for local entrepreneurship in developing countries.

This policy review indicates that there are country-specific situations and programme activities in which both these incentives converge (PSOM/PSI, ORET). The decision to open up the PSD instruments to an extremely broad group of 66 developing countries – with strongly diverging levels of development and economic dynamics – has created several dilemmas.[11]

For the time being, many of the poorest countries (such as Mali, Rwanda and Mozambique) still have limited appeal for the Dutch business sector as a result of their restricted markets and high risk factor, especially when it comes to direct investment. In light of the ratio between the size of total foreign investment (FDI) and total aid (ODA), most of the added value of public support for private sector development lies in these kinds of countries.

[11] The latest list of developing countries eligible for the PSD instruments consists of 66 developing countries, whose levels of income vary from the Democratic Republic of Congo's (GNP US$ 231 per capita in 2011) to Suriname's (US$ 8,131 per capita). Colombia's GNP per capita is 18 times that of Burundi's, while Thailand's GNP (US$ 4,972 per capita) is 10 times that of Uganda's, and Indonesia's GNP (US$ 3,495 per capita) is 10 times that of Ethiopia's. In addition to 22 low-income countries (roughly < US$ 1,000 per capita), the list contains 27 low middle-income countries (US$ 1,000 - US$ 4,000 per capita), 12 high middle-income countries (US$ 4,000 - $ 12,000 per capita) and five countries for which there is no information about GNP per capita at the World Bank (generally poor countries and conflict areas).

In developing countries with a somewhat higher level of income, the importance of development cooperation generally decreased because some degree of foreign (and domestic) investment is often secured there without public support. In many cases, these are countries that harbour more substantial opportunities for the Dutch business sector.

Some middle-income countries on the Dutch PSD list are already so developed (such as Thailand, India, South Africa and Colombia) that one could ask whether state support (Dutch) for private investments or provisions are still additional. Market distortion is a potentially greater threat in these countries, in part because of the wider availability of market-based financing. Should the Dutch government still intervene with public resources earmarked for the private sector in countries that have already experienced considerable market development? Without setting exact boundaries in advance, the policy could take more into account the relationship between a country's level of development and the desirability of using public support for private activities, even if this support aims to benefit the Dutch economy.

The type of public financing deserves attention as well. It is generally more desirable to give grants to the poorest countries because the business risks are much higher there, and it is undesirable to build up (publicly guaranteed) debt. Concessional loans should go to countries with higher levels of development, to the extent that market-based loans on reasonable conditions are not yet available there. What would be worth considering is fine-tuning the degree of concessionality of PSD instruments to the local circumstances in order to diversify this highly focused set of instruments.

2. More harmony in order to achieve greater synergy

The Dutch PSD policy aims to concentrate on priority themes, but at the same time has a broad range of instruments, a long list of countries and activities tailored to almost every bottleneck in private sector development in the five policy clusters. The policy review has established that there is little to no synergy at the country level between the instruments, which are usually centrally implemented with little guidance from The Hague and by the implementing organisations. More focus is needed to increase policy coherence.

Increasing the synergy of the PSD instruments at the country level can be promoted in several ways. Partner countries and embassies could play a more significant role during the identification and selection phase of a number of PSD programmes, especially in clusters such as infrastructure, financial sector development and market development. One condition, however, is that the ministry builds sufficient capacity and expertise in this area. An alternative is to promote far-reaching cooperation between implementing organisations in a country, in which the embassy takes on a coordinating and facilitating role. In addition, what is worth considering is using the PSD instruments more often simultaneously or sequentially to address the specific constraints that businesses face during the various development phases. Furthermore, reducing the number of instruments and concentrating the PSD resources in a limited number of countries would increase the effectiveness of Dutch efforts.

3. Professional commissioning and functional management

The targeted use of PSD instruments requires a great deal of information, knowledge and skills in order to adequately tailor decision making about financing conditions for the various instruments to both demand in developing countries and supply in the private sector.

Professional commissioning by the ministry would benefit from a more elaborate assessment framework for individual instruments, in which the criteria and conditions for the use of resources are more precisely specified. This would also clarify the frameworks for independent administrators of the programmes. These administrators would be judged on results achieved (results-based management) and not only on activities undertaken.

1

Introduction

This chapter describes the approach used in this policy review. What was the objective? What were the main research questions? How is the policy area defined? What is the evaluation study's methodological approach, and what are its limitations? The chapter concludes with a note on the structure of this extensive summary of the original report in Dutch.

Motivation and objective

Strengthening the private sector in development countries has been one of the objectives of Dutch development policy for a long time. The significance of this activity has increased in recent years and was an important reason for IOB to launch a study on the impact of Dutch policy on private sector development.

In addition, the ministerial decree on performance measurement and evaluation (RPE) requires that all policies be evaluated by means of a policy review with a certain amount of regularity. This kind of review has two purposes: (a) it provides an overview of the degree to which the policy area in question has been evaluated, and (b) based on that, it assesses the effectiveness and efficiency of the instruments used in conjunction with each other (Staatscourant, 2012b). In addition to increasing insight on the functioning of the policy (what works and what does not?), the study also aims to lay the foundation for accountability to the Dutch parliament.

Research questions

The main research question concerns the relevance and effectiveness of Dutch policy for private sector development in developing countries. It has been broken down into the following elements:

- *Description and analysis of the problem that motivated the policy.*

This element examines the bottlenecks in private sector development in developing countries and the relevance of the Dutch business sector programme.

- *Description of and reasons behind the Dutch government's involvement.*

This element looks at the reasons for the Netherlands to strengthen the general entrepreneurial climate and offer support to individual companies and sectors. The additionality of the government intervention receives special attention.

- *Description of the policy objectives under scrutiny.*

This element analyses the policy's division into five thematic clusters and indicates which intervention logic was used.

- *Description of the instruments and analysis of their social impact.*

This occurs in the study by means of an analysis of the instruments within each cluster, with special attention going to the instruments' scope and the effectiveness. The coherence and potential overlap of the various instruments is also examined.

- *Description of the budget that was used.*

This element consists of an analysis of the distribution of the PSD budget across the various programmes and projects, and an assessment of the scope of the guidance and management of these programmes.

For easy reference, IOB has chosen to treat the research questions in conjunction with one another.

Scope and source materials

The evaluation covers the policy and expenditures of the Ministry of Foreign Affairs during the period 2005-2012 in the area of support for private sector development in developing countries. IOB has chosen to structure the study in a number of clusters, in line with the division used by the Ministry of Foreign Affairs.The five PSD clusters are infrastructure, financial sector development, market development, knowledge and skills, and laws and regulations. In addition, the report also deals with public-private partnerships (PPPs) and the theme of international corporate social responsibility (ICSR).

The policy review resembles a synthesis study: it summarises what is known about the social impact of the policy based on the outcomes of existing impact studies. Comparing outcomes to the policy objectives makes it possible to assess the degree of the policy's effectiveness.

Preliminary research has shown that when the policy review began there were more than 100 evaluations and reviews of PSD programmes and projects available at the ministry. Most reports, however, did not contain valid (does the study actually measure what it purports to measure?) or reliable (how stable are the study outcomes?) impact assessments. As a result, IOB has conducted a number of separate, supplementary studies.

Approach and limitations

The approach is based on a combination of theory-based and evidence-based evaluation. That means, among other things, that IOB examined the policy report's relevance and the reported results against the background of the international literature on the subject. This approach helps to increase the external validity of the findings (the likelihood that outcomes could be achieved under other circumstances).

The study consists of four parts. First, a reconstruction of Dutch policy. The report deals with PSD policy against the background of the international policy debate about the role the private sector can play in promoting growth and poverty reduction in developing countries.

Second, the review also contains an overview of the expenditures (2005-2012) for each of the five policy clusters, the findings regarding the policy's relevance and the effectiveness of the instruments. The objective of this was to gain insight into the impact of the PSD instruments.

Third, country studies were conducted in Bangladesh, Burundi, Ethiopia and Vietnam. These field studies contain a description of the post's policy, an analysis of its implementation and an estimate of the perceived and achieved impact of Dutch support to the development of the private sector in the country in question. In doing so, the country studies devote attention to the coherence of the different centralised and decentralised instruments in the area of private sector development.

Fourth, IOB has conducted a systematic review of the literature on the impact of government interventions in the area of international corporate social responsibility and the results of public-private partnerships in development cooperation. IOB has published both these studies separately.

The findings from this review are based on a combination of source material, project files, field observations, interviews and international studies on the impact of similar programmes. The assessment of IOB's impact used existing evaluations of the various instruments. IOB did not conduct its own effectiveness study. The study focuses on the more significant expenditures. Minor activities carried out by the ministry, such as activities related to increasing knowledge or international cooperation in the area of PSD therefore receive little or no attention.

Structure

This emphasis of this summary of the original Dutch report is on describing international policy (chapter 2) and the findings of the review of international literature (chapter 3). Chapter 4 contains a much-shortened version of the description of Dutch policy, PSD expenditures, the use of instruments and what is known about their impact.

2

Private sector development in international development cooperation policy

From import substitution to the Washington Consensus

The emphasis in many developing countries during the 1960s and 1970s lay on economic development managed by the government, with a larger role for semi-public and public companies. These countries often followed an 'import substitution' strategy. Backed by analyses by development economists such Raul Prebisch (1950) and Hans Singer (1950), governments in Latin America, Africa and South Asia encouraged capital-intensive industrialisation. In doing so, they protected the national business sector from competing with Western countries dominated by global trade. Countries such as former Zaire, India and Senegal set up their own car industries after independence, while Indonesia focused on shipbuilding in the 1960s and Egypt invested in steel production and chemistry (Lin, 2012b). These companies often operated on government support and were not viable in the long run.

In the early 1980s, the Anglo-Saxon neoliberal way of thinking about the role of the free market and private initiatives in economic development in developing countries began to gain currency (Estrup, 2009). The World Bank, the International Monetary Fund (IMF) and bilateral donors (led by the United States and the United Kingdom) pushed for a package of drastic reform, which became known as the Washington Consensus. It perceived government intervention as the core of the problem and advocated less state involvement in favour of allowing market forces and corporate production to overcome stagnation, especially in sub-Saharan Africa (World Bank, 1981). The 1980s and 1990s saw the introduction of the structural adjustment programme of economic and financial liberalisation, the privatisation of state companies and the rigorous reorganisation of government spending in dozens of developing countries that had approached the IMF and the World Bank for concessional loans to keep the countries running.

Reassessment of the state's role

The growth impact of the structural adjustment programmes was disappointing, especially in the poorest countries. The privatisation of companies and government agencies often resulted in failure (Independent Evaluation Group, 2005). In many countries, the social impact of drastic government cutbacks, layoffs and the shock of privatisation and liberalisation was severe and generated increasing resentment. The UN responded by calling for 'adjustment with a human face' (Cornia et al., 1987). The financial crises that successively hit Mexico, the Asian Tigers, Russia and Argentina also raised doubts about the liberalisation of the financial markets, one of the pillars of the Washington Consensus (Rodrik, 2011).

Various movements within the World Bank had been struggling since the early 1990s to explain how East Asian countries such as South Korea, Taiwan, Singapore and Hong Kong could have emerged so quickly.[12] After all, the strong growth of the private sector in these countries had been achieved with a relatively large amount of government support and protection, against the grain of the Washington Consensus. Criticism increased at the World

[12] See Page, 1993, *The East Asian Miracle: Four Lessons for Development Policy*.

Bank in the late 1990s. In 1998, the chief economist at the time, Joseph Stiglitz, called the Washington Consensus 'at best incomplete and at worst misguided' and called for a new paradigm (Stiglitz, 1998). There had to be a great deal more focus on the unique functions of the public sector for creating an 'enabling environment' for the private sector. Education and health care were part of that as well.

The turn of the century witnessed the gradual development of a Post-Washington Consensus that explicitly recognised the supporting role of governments and public institutions in facilitating private sector growth. In 2002, the World Bank put down on paper for the first time a detailed strategy for private sector development that emphasised the complementary functions of the state and the private sector.

The strong emergence of the BRICs (Brazil, Russia, India and China) and other non-Western G20 countries in the new millennium ate away at the global dominance of Anglo-Saxon neoliberal development philosophy – certainly following the 2008 credit crisis (Birdsall and Fukuyama, 2011). Important basic tenets, such as the liberalisation of the capital market and refraining from formulating an active industrial policy, were no longer seen as a panacea in a multipolar global economy. Former chief economist at the World Bank, Justin Lin, pointed out that none of the developing countries that posted high growth figures for years observed liberal policies closely; instead, they used a pragmatic mixture of market forces and a proactive facilitating government (Lin, 2012a). Based on this experience, Lin argues in favour of changing the growth concept for developing countries. He sees the government taking on an active role in this concept, including a coordinating role in setting up infrastructure and implementing a targeted industrial policy based on comparative advantages that are present from the start (Lin, 2012b). Market forces and private entrepreneurial production remain the basic tenets, however.

Towards a broad approach to private sector development

Direct support to companies was part of the arsenal of strategies in OECD countries in the early years. Certainly in the first decade (1950-1970), aid was often linked to provisions from the business sector or support from subsidiary enterprises in the donor countries. The World Bank was involved in operating aid because it provided loans to governments and financial intermediaries guaranteed by governments, in order to support state companies and private enterprises (IOB, 2013e). In 1956, the International Finance Corporation (IFC) was founded as part of the World Bank Group, with the specific task of financing private enterprises in developing countries.

A much broader approach to private sector development became an explicit part of the set of instruments of development cooperation from the 1990s onward (Schulpen and Gibbon, 2002). In 1995, the OECD's development assistance committee (OECD-DAC) published *Orientations for Development Co-operation in Support of Private Sector Development*. The document discusses the reversal in thinking in many developing countries – following decades of central planning and management of production by the government – regarding private initiatives and market forces. Donors would have to respond accordingly and actively support this process of change in developing countries. Actions taken by donors would have to focus on promoting an enabling environment for the private sector, financial reform, privatisation and providing support to businesses through the transfer of knowledge.

The World Bank Group presented a broad strategy for PSD in 2002 (World Bank, 2002). Improving the investment climate by removing 'unjustified obstacles to private business' was the strategy's core message. The International Bank for Reconstruction and Development and the International Development Association were to focus on strengthening competition policy, adapting laws and regulations, reforming the financial sector and securing property rights. The World Bank would report on progress in these areas in the annual *Doing Business* report, which appeared for the first time in 2003. The World Bank would continue to give direct public support to entrepreneurs via IFC, including microcredit.

The title of the *World Development Report 2005*, 'A Better Investment Climate for Everyone', further underpinned the importance of private sector development (World Bank, 2004). A major study involving tens of thousands of poor people (*Voices of the Poor*) revealed that they viewed a job or having their own business as by far the two best ways of escaping poverty. Private enterprises, from independent smallholder farmers to multinationals, provided 90% of all employment in the world. They were the most important source of tax revenue, necessary to finance public services such as health care and education. A flourishing business sector was crucial for growth and poverty reduction.

The investment climate – defined as 'the location-specific factors that shape the opportunities and incentives for firms to invest productively, create jobs and expand' – was for a large part determined by the policy and behaviour of governments, according to the World Bank report. The report warned governments not to go too far beyond these basics of a good investment climate. Interventions to encourage specific businesses, sectors or (foreign) investment by means of tax exemptions, subsidised credit or market protection had failed too often, according to the World Bank. The experience with selective support of businesses ('picking winners') had fallen short and often came down to gambling with scarce public resources. If the choice were to fall on this type of support, then the objectives would have to be formulated extremely clearly with straightforward conditions for the beneficiaries, and implemented in a completely transparent way with regular impact assessments.

Pro-poor growth and employment opportunities

In the same period, OECD-DAC published a new outlook on the relation between private sector development and poverty reduction and the role played by donors (OECD, 2004, 2006). Pro-poor growth, the growth of the incomes of people with an income below the poverty line, had to be achieved by improving the conditions for private sector development and, within these conditions, promote models that create opportunities for the poorest groups. The crux of the matter was promoting pro-poor market outcomes, such as more and better jobs, higher incomes, higher yields for the products of the poorest people and more affordable essential goods and services. Donors should not focus their efforts on direct interventions for the benefit of the poorest groups (such as subsidised microcredit), but encourage the market to respond to the needs of the poorest groups (mainstream microcredit in the commercial banking system): 'changing the incentives within markets to deliver pro-poor outcomes rather than providing direct support to enterprises' (OECD, 2006). Direct interventions often disrupted the market and were rarely sustainable. Institutional and policy reforms had to become the core of the new donor approach to private sector development.

The *World Development Report 2013* approaches private sector development from the angle of employment. High unemployment (such as is North African countries, and especially among young people) and economic growth without job creation are current challenges that require more emphasis on employment policy. Jobs not only raise the living standard and increase production, but they also strengthen social cohesion. In addition to promoting the basic conditions for PSD – macro-economic stability, a good investment climate, the accumulation of human capital and legal certainty – the World Bank also believes there is a role for governments in the area of labour market policy. Indeed, the report goes one step further regarding government interventions to stimulate economic activity when the World Bank talks about a targeted investment climate, i.e. targeted government action that is sometimes necessary to tackle market failure and institutional weakness. This marked the return of the proactive government in mainstream development thinking.

3

International literature on private sector development

Chapter 3 examines information in international literature about bottlenecks in private sector development in developing countries and what potential solutions the literature offers for these bottlenecks. This chapter follows the same division into five clusters used in Dutch PSD policy, namely: infrastructure, financial sector development, market development, knowledge and skills, and laws and regulations.

3.1 Infrastructure development

Infrastructure and economic growth

An increasing number of econometric studies emphasise the highly positive impact of infrastructure on economic growth (Hulten, 1996; Esfahani and Ramirez, 2003; Calderón and Servén, 2004; Willoughby, 2004; Calderón, 2009). According to Hulten, imbalances in infrastructure account for more than 40% of the growth differences between countries and 25% of the growth differences between Africa and East Asia (see also Ndulu, 2006). Lederman et al. (2005) discovered that good infrastructure is crucial for the success of measures aimed at promoting free trade and exports. Good infrastructure also has a positive impact on foreign investment (Asiedu, 2006). In particular, (mobile) telephony, roads, electricity and railway lines have a major impact on economic growth (Calderón and Servén, 2004; Calderón, 2009; Ferro et al., 2011). Calderón (2009) analysed the impact of investments in infrastructure on economic growth in Africa for the period 1960-2005. The author concludes that they had a greater impact on economic development than other structural policy measures (about 45% higher).[13] Foster and Briceño-Garmendia (2010) conclude that infrastructure, and telecommunications in particular, accounts for more the 50% of recent economic growth in Africa. Africa lags behind in other areas, however, partly as a result of what are frequently difficult geographic circumstances (see, for example, Calderón, 2009; Ndulu, 2006, 2007; Foster and Briceño-Garmendia, 2010). Improving the availability (and reliability) of electricity remains the biggest challenge. Poor infrastructure has direct consequences for the development of the private sector and therefore a negative impact on private investment, in part as a result of power outages and impassable roads (WSP International Management Consulting, 2007).

Providing the poorest people with access to infrastructure can also help to reduce income imbalances, providing the investments are targeted (Calderón and Servén, 2004; Terberger et al., 2010). Improving infrastructure has a positive impact on access to education and health care, reduces production and transaction costs, and improves labour market participation (Calderón and Servén, 2004; Foster and Briceño-Garmendia, 2010). The cost of investing in rural areas is often relatively high (as a result of diseconomies of scale; see Willoughby, 2004). The anticipated trickle-down effects of economic growth, however, often turn out to be disappointing (OECD, 2006; WSP International Management Consulting, 2007; Terberger et al., 2010).

[13] Ninety per cent of this can be attributed to the expansion of the infrastructure and ten per cent to improved quality.

One of the biggest bottlenecks for investing in infrastructure is a lack of capital. Partly as a result of the financial crisis, international banks have no longer been willing to finance risky infrastructure projects in sub-Saharan Africa in recent years. But a lack of capital is not always the only problem. Various reviews show that the lack of high-quality projects is often a core problem. Too many risks prevent project developers from putting time and money into projects, and as a result they never get off the ground (PIDG, 2009). Until now, private investors have really only been willing to invest in mobile telephony, power plants and container terminals.

Indeed, some of the present problems are the result of poorly allocated public resources. Foster and Briceño-Garmendia (2010) conclude that African countries can save approximately US$ 17 billion by spending resources more efficiently. More than US$ 3 billion goes to sectors that do not need it. Several governments invest too much in ICT infrastructure, for example. The private sector can handle this investment, especially in many middle-income countries. Countries can also avoid the high costs of repair through better maintenance.

Transport

Bad roads are especially a problem in landlocked countries (Ndulu, 2006; Foster and Briceño-Garmendia, 2010). Transport costs are high in these countries, and the opportunities to engage in trade are limited (Ndulu, 2006). But other countries face these problems as well. Until recently, the Democratic Republic of Congo did not have more than 2,200 kilometres of paved roads. During the rainy season, many roads are impassable. Bad maintenance is a problem with many roads in sub-Saharan Africa. Donors have often financed road repairs, just to see these roads in disrepair again a few years later due to lack of maintenance (Oxford Policy Management, 2008). Investments (private or otherwise) in roads are often not economically viable as a result of relatively moderate use and the extremely limited resources of many users. This is especially true for railway systems, where maintenance and repair costs are high. Local contractors rarely have sufficient capital at their disposal to prefinance road building or maintenance. Ambiguous and unreliable procurement rules and exchange rate risks are factors for foreign investors. Bad roads are another obstacle for the improvement of other infrastructural facilities. For instance, the price of many infrastructural facilities in the above-mentioned example of the Democratic Republic of Congo is twice as high as elsewhere (Briceño-Garmendia & Foster, 2009).

Research by the Asian Development Bank (Hettige, 2006) and DANIDA (2010) highlight the positive economic and social impact of secondary roads for rural development. ADB concludes that improving roads is a necessary, though not sufficient, condition for rural development. The DANIDA evaluation suggests that these roads increase the level of paid employment and reduce travel time to social services outside the immediate community. Comparative studies of investments in poverty reduction show that the greatest impact is in agricultural research, education *and* investing in roads (Willoughby, 2004). An evaluation by KfW for Zambia reveals that investing in roads in rural areas has an impact on both income and enrolment in education, especially in secondary education (Terberger et al., 2010).

A poor port infrastructure can also constitute a major obstacle to economic development. In 2007, ships in Dar es Salaam remained in port an average of 12 days before they were unloaded; it took an average of 27 days before ships were loaded and could continue on their journey to transport goods. As a result of these delays, shipping through Dar es Salaam costs 25% more than in comparable ports in South Africa. Countries such as Uganda and Rwanda, which are landlocked, suffer from this as well. According to Oxford Policy Management (2008), ports are one of the areas in which private investment is successful. The legal framework is often clear, permits are easily obtained, projects are relatively small scale and can be easily earmarked, and the income is often in foreign currency, enabling investors to avoid exchange rate risks. Often, there are also clear opportunities to improve efficiency so that private investors can make relatively high profits, and as a result they are willing to pay substantial amounts for permits. Airports, on the other hand, sometimes lack the volume to be economically viable.

Electricity

A shortage of energy, especially electricity, is one of the biggest bottlenecks in Africa for many businesses, and as a result it is the most important factor limiting growth. The 48 countries in sub-Saharan Africa produce as much electricity as Spain, but they have 18 times more inhabitants (Briceño-Garmendia and Foster, 2009). In many countries, especially in Africa, electricity companies are state-run, or were until recently. For many reasons, these companies invested far too little to meet the increasing demand, and they were not managed effectively or efficiently to boot, which resulted in an unreliable electricity grid (in Tanzania and Uganda, for example) and forced entrepreneurs to buy backup generators. The sector has little appeal for commercial entrepreneurs, especially as a result of ambiguous and unreliable planning and procurement procedures, which lead to long-term risk (Oxford Policy Management, 2008). Development banks, such as FMO, invest heavily in that sector.

White (2008) concludes that, in addition to a positive development impact, investing in rural electrification can be sufficiently viable as well, providing the electrification is adapted to the specific (local) circumstances. He also points out, however, that these projects rarely have the explicit goal of reducing poverty. As a consequence, it is generally the non-poor that profit most from rural electrification. The poorest usually cannot afford to get connected, and when they can they receive insufficient information to benefit from being connected.[14] Although electrification has a positive impact on the number and size of businesses in rural areas, research shows that this impact is often overestimated (White, 2008; IOB, 2013d).

Telecommunications

Mobile telephony is booming in Africa. In 1999, 10% of the population had access to a mobile network; in 2008 that had already increased to 65%. There are still significant gaps,

[14] White cites two examples. First, it is common in villages that have been connected to the electricity grid for 15-20 years for 20% to 25% of the households to not be connected; second, it is not always clear to the poorest users that they pay a fixed, minimum rate for the first 25 kWh per hour, so that they cut back on electricity use even though it does not affect their bills.

however: coverage in North Africa is 93% whereas in sub-Saharan Africa it is 60% (in 2008; see Aker and Mbiti, 2010). Together with ports, mobile telephony is one of the sectors that attracts the most private investment. One of the reasons for this is the use of prepaid cards, which makes it easy to disconnect people who default on their payments. Other, partly related factors include a relatively low level of investment, a low user threshold and high profitability. The absence of landlines has also contributed to the rapid expansion of mobile telephony in Africa. The coverage in sparsely populated rural areas, however, remains a problem.

Investing in mobile telephones has had a positive impact on agriculture, the labour market and economic development in developing countries, according to various researchers (Torrero et al., 2005; IOB, 2009). According to Calderon (2009), it is telecommunications in particular that has contributed to economic growth in Africa in recent decades, much more so than other sectors (such as energy and roads), which – measured over the entire period – barely improved. Estimates for Africa vary from 1% to 5% of GDP (Harrison et al., 2013; IOB, 2009). In a survey, entrepreneurs in Tanzania cited mobile telephony as the most important contributor to regional market development (Song, 2006). Waverman and Meschi (2005) calculated the impact of mobile telephony on economic growth in Africa to be twice as high as in developed countries. The impact of mobile telephony can be especially significant in rural areas (Bhavnani et al., 2008).

Water and sanitation

Water and sanitation, like energy, are often state-run. These public utilities often function poorly and generate barely any investment finance, if at all. Private investors should essentially be able to contribute significantly to more efficient business operations, but that is barely the case. Few companies operate in that sector. The most important reasons are that projects are capital intensive and have an extremely long payback time. There is a lack of water metres, and as a result there is not a single incentive to cut back on use. The price and disconnecting users who default on their payment are politically sensitive matters.[15] Oxford Policy Management (2008) concludes that water and sanitation are among the least appealing sectors for private investors. Private projects usually prefer management contracts to making sizeable investments. Successful investment depends on substantial donor contributions in tandem with political will in the host country (see also IOB, 2012b).

The use of improved water sources has increased considerably, but that has not guaranteed safe or adequate amounts of drinking water (IOB, 2012b). A major problem is that households continue to use unsafe sources as well, or they transport and store water in contaminated jerrycans. Evaluations by KfW (2010) and IOB (2012b) show that rural drinking water facilities have a positive impact on enrolment in education. But the KfW evaluation also reveals that it is mostly (bilateral) donors and NGOs who operate in rural areas. Governments focus much more on providing safe drinking water and sanitary facilities in

[15] Although in Zambia, for example, schools are disconnected because they cannot pay public utility service bills.

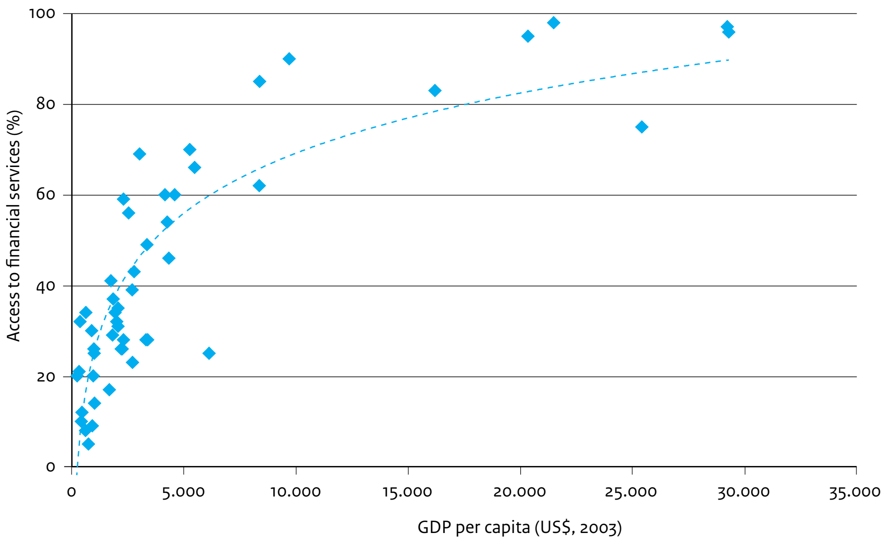
cities. IOB and KfW conclude that poor communities do benefit from improved drinking water facilities, but the very poorest communities benefit less. Sanitary facilities have improved, especially in less poor regions. They are often too expensive for the poorest households.

3.2 Financial sector development

Financial services and economic growth

There is a close correlation between financial infrastructure and economic development. In countries with a high income per capita, there is substantially better access to financial services than in countries with lower incomes (see figure 1).

Figure 1 *Access to financial services by income*



Source: World Bank, 2008 (elaborated on by IOB).

Providing credit is an example. The least credit is provided in sub-Saharan Africa, varying from less than 2% of GDP in Mozambique to approximately 25% in Kenya (Beck et al., 2008). In developing countries that figure can exceed 100%. Economic growth increases the demand for financial services. According to a growing number of publications, not only do better financial services arise from economic development, but they also contribute significantly to it. According to Claessens (2006), international comparative studies identify financial infrastructure as one of the few robust determinants of economic growth (see also World Bank (2008). Countries with a well-developed financial sector had higher average economic growth per capita between 1980 and 2007 than countries with a less well-developed financial sector (Beck et al., 2011). The relationship between the two is complex, however, and the direction of the causality is difficult to determine, though increasingly researchers are using techniques that make it possible to solve this problem of reverse causality.[16] Nevertheless, the literature is not unanimous on this point. Liang and Teng (2006) conclude for China that there is only a casual relation from economic growth to financial development but not vice versa. On the other hand (Jun, 2012), there is a positive and statistically significant mutual relation between financial development and increased production.

Well-functioning financial systems can contribute to economic growth by mobilising capital and reducing communication and transaction costs (Levine, 2005). Better developed financial markets reduce the cost of external financing. As a result, it is easier for businesses to invest at a lower cost. Claessens and Feijen (2006) cite the considerable influence that the financial sector has on improving productivity. A well-developed financial sector fosters technological innovation and promotes greater competitiveness. Countries whose financial Sectors are more developed enjoy greater technological progress, a strong reduction in production costs and higher productivity growth. It also appears that capital-intensive industries in countries with a well-developed financial system have relatively high growth figures (Zhuang et al., 2009).

According to various researchers, thriving financial markets also contribute to more equal distributions of income and reduce poverty (Claessens, 2006; Clarke et al., 2006; Beck et al., 2008; World Bank, 2008; Zhuang et al., 2009). Conversely, poorly functioning markets can perpetuate inequality, poverty and weak economic growth. Indeed, banking systems and capital markets in developing countries focus on the wealthier part of the population and on the larger businesses (Claessens, 2006; Levine, 2005). The absence of financial resources and poor financial services means people will not have the opportunity to start up a business and companies will not have room to grow. A flawed financial infrastructure therefore impedes economic development (Ndikumana, 2000; Levine, 2005; Claessens, 2006; Beck et al., 2008; Ayyagari et al., 2008; Beck et al., 2011). Research also shows that poverty levels decrease in countries with more developed financial systems (Mavrotas and Son, 2006; Beck et al., 2011). Incidentally, this is usually achieved through trickle-down effects and much less through improving access to financial services for the poor (Karlan and Morduch, 2010).

If a thriving financial sector is so important for economic growth and poverty reduction, then one has to wonder why this is not happening in developing countries. The literature (see, for example, Levine, 2005; Claessens, 2006; Beck et al., 2008; IFC, 2011) cites several explanations: demand, supply and institutional factors. In practice, these are all closely related. The factors that impede access to a bank account or credit include:

[16] It mainly concerns the use of instrumental variables. Another approach is that of Beck et al. (2011), who examine the relationship between existing financial systems and the ensuing economic development.

- Physical distance, the absence of local infrastructure. A country like Spain has one bank branch for every 1,000 inhabitants and eight per 100 km^2; Ethiopia has one branch per 100,000 inhabitants and Botswana one per 10,000 km^2 (World Bank, 2008);
- Financial barriers, such as high costs or a minimum charge to open a bank account; and
- Formal requirements, such as a valid ID or a salary slip. There are additional requirements for a loan, such as proof of a fixed income and/or collateral.

The obstacles to the development of the financial sector, especially in Africa, are essentially the reciprocal of the above-mentioned factors (Claessens and Feijen, 2006; Beck et al., 2011):

- The small scale of many (African) economies and the low population density means providers are unable to take advantage of economies of scale. Service provision outside urban centres is therefore usually unprofitable;
- Connected to this is the low income of a large part of the population, and related to that, a low savings rate;
- The relatively high costs – including for financial institutions – for small bank accounts or loans, which can be higher than the initial deposit, the average balance or the size of the loan request;
- Large parts of (African) economies (40%-60%) are in the informal sector.[17] People working in this sector often do not possess the required documents, such as business registration, proprietary rights or even a formal address; and
- The insecure and fluctuating incomes of potential borrowers means loans are by definition high risk.

The following macro-economic and institutional factors also have a negative impact on the development of the financial sector (see also Calice, Chando and Sekioua, 2012):

- Macro-economic instability (inflation and exchange rate risks) creates considerable risk, as a result of which banks (have to) ask for substantial margins;
- The absence of adequate regulation and its enforcement, which would require borrowers to meet their obligations;
- Bottlenecks in government administration: poor legislation, insufficient respect for the rule of law, corruption and political interference increase financial risks; and
- Significant capital flight, which contributes to the scarcity of capital.[18]

These obstacles are especially significant in Africa. They are one of the reasons why short-term thinking dominates the African banking system, where 80% of deposits and 60% of loans have a term of less than a year (Beck et al., 2011). The problems are also reflected in high interest rates. For many potential customers, the high minimum charges (for opening an account as well as taking a loan) and the high costs are prohibitive. The above-

[17] These 'micro-enterprises' often only exist because of a lack of economic alternatives (Beck et al., 2011).

[18] This capital flight has decreased significantly in recent years, which could mean there is growing confidence in local finance systems (ibid.).

mentioned obstacles are especially high hurdles to face for small farmers in rural Africa (Beck et al., 2011).

Multilateral and bilateral donors refer to their attempts to tackle the financial infrastructure problems as 'financial inclusion'. The concept means universal and sustainable access, at a reasonable cost, to a range of financial services, such as opening a bank account, ability to make payments by giro, a savings account, credit and insurances. The fundamental idea is that access is extremely important for creating opportunities for people to engage in financial transactions, spread risk, save for a pension and deal with emergencies, such as illness. It is estimated that 2.5 billion people still do not have access to formal financial services. The G20 put the issue on its agenda during the summit in Seoul in December 2010, and among other things it launched a Global Partnership for Financial Inclusion (GPFI). In 1995, the World Bank founded the Consultative Group to Assist the Poor (CGAP) in order to find innovative ways – by means of research and cooperation with providers of financial services – to remove the obstacles that prevent the poorest from accessing financial services. The World Bank has set itself the aim of ensuring that all adults have access to formal financial services by 2020. The bank is relying mainly on technological innovations to remove obstacles that prevent access to financial services (World Bank, 2013). The Netherlands is contributing to these initiatives as well, for example by participating in the financial working group for small and medium enterprises of the GPFI, the World Bank's Global Agriculture and Food Security Progam (GAFSP) and working groups in the area of financial education (OECD) and consumer protection (FinCoNet).

Recent research suggests that significant progress has been made in this area. In the World Bank's Global Financial Barometer (2012a), 78% of financial service providers responded by saying that financial services in their country had improved considerably over the past five years.

Businesses

International comparative research on the most important factors preventing businesses from growing invariably cites the lack of access to capital as the primary factor, ahead of corruption, political instability and poor regulation (Ayyagari et al., 2008; World Bank, 2008). The only bigger obstacle than access to financing is the absence of a reliable electricity supply (IFC, 2011). High interest rates (on average 17%, as opposed to 12% outside Africa) mean that a loan is only cost-effective if there is a high yield on investment. Cumbersome procedures are a much more common reason in Africa (18%) for not granting a loan than outside Africa (7%); coming up with collateral is an obstacle twice as often (10% versus 5% outside Africa; Beck et al., 2011). Conversely, banks often have insufficient information at their disposal about customers, and they do not have the option of asking for collateral.

Small formal and informal businesses in particular have difficulty opening accounts or applying for credit. These businesses play an important role in developing countries. Three out of four formally registered micro-businesses and SMEs have one to four employees (World Bank, 2013). These are mainly small family businesses (Calice et al., 2012). When the reverse is true, it usually concerns informal businesses: 80% of micro-businesses and SMEs are not formally registered. It is precisely these businesses that make little use of formal financial services, such as bank accounts (Farazi, 2013). A large majority uses informal channels, including moneylenders, family and friends to finance operational costs and investments. The use of a bank account among registered businesses is 54% higher; the availability of formal credit is on average 32% higher.

An important reason why farmers make so little use of the financial infrastructure is the geographic distance to banks. Moreover, a lack of trust in banks, unreliable services and high costs for withdrawing money also play a role (World Bank, 2012a). The nature of the farming business, with many uncertainties (especially susceptibility to weather conditions), is a third factor. The latter means that insurances could play a part in limiting risk. In the absence of formal possibilities for using financial services, famers are often forced to resort to informal instruments. Moreover, the resources are often inadequate for introducing new technologies or acquiring a sufficient number of necessary inputs.

Because smaller and medium-sized businesses in particular have difficulty financing their investments, they also stand to benefit the most from a well-developed financial sector (see Claessens and Feijen, 2006; Beck et al., 2010). In that respect, Calice et al. (2012) argue that a stable macro-economic environment, predictable government policy and legislative reform are the most important conditions for increased loan provisions to small and medium enterprises.

Better access to capital contributes to a rise in the number of start-up companies, better investment opportunities, higher productivity and more efficient production, which also make businesses more competitive. Heavy interest burdens play an important part, but these are closely correlated to other factors, such as demand for security (collateral), bureaucratic requirements, corruption in the banking sector and a lack of opportunities for long-term borrowing. The World Bank (2013) concludes that strengthening property rights and enforcing contracts can help to improve farmers' access to credit. Because much poverty is concentrated in rural areas, giving farmers access to credit can also help reduce poverty. Research shows that increased productivity is precisely one of the factors that reduces poverty and that growth in the agricultural sector causes poverty levels to decline. De Kemp, Faust and Leiderer (2011) conclude in a study of budget support in Zambia that poverty barely decreased despite economic growth because it essentially bypassed (rural) agriculture. Other studies confirm this contention (IOB, 2012a). The World Bank concludes that reinforcing property rights and legislation can help to improve farmers' access to credit. Critics, however, point out that financing is only one of the many problems that businesses face, and that knowledge of modern technologies and access to markets is equally important (Zhuang et al., 2009; World Bank, 2012a)

In 2008, IEG published the findings of a study on the results of IFC's support of financial intermediaries (banks) that provide credit to small, medium and micro-enterprises in low-income countries and high-risk countries. The evaluation is largely positive and concludes that on average the projects achieved excellent development outcomes – higher than other projects in these countries.[19] These development outcomes, however, mainly concern the intermediary institutions that received direct financing. The evaluation provides much less insight into the impact on the welfare of the ultimate beneficiaries.

Microcredit

Because poorer households have barely any access to credit, they are more vulnerable to fluctuations in their income and also experience these fluctuations more frequently (for example, in subsistence farming and other forms of informal labour). That indicates the importance of mechanisms that absorb these fluctuations, such as the possibility to save and to borrow. Microcredit received a great deal of attention in particular.

The history of modern microfinance can be traced back to Nobel Prize winner Muhammad Yunus' Grameen Bank in Bangladesh in the 1970s. Partly thanks to the successes that he claimed with loans to the poor in rural areas – and supported by a number of positive evaluations – microfinance grew into a mega-industry. It is estimated that in 2009 this industry turned over US$ 23 billion (Aggarwal et al., 2012). Today, microfinance encompasses a whole range of financial services, including micro-bank accounts, micro-saving and micro-insurance. Microfinance institutions (MFIs) now reach almost 200 million people (Bauchet et al., 2011). By providing groups with the lowest incomes and micro-businesses access to credit, microfinance could achieve various goals:

- Loans would enable the poorest segments of the population to start their own businesses;
- Existing (informal) micro-businesses could invest more, which would allow them to grow;
- Both factors lead to better employment opportunities and a positive impact on income;
- Which can affect other consumption patterns (including increased spending on education for children); and
- Microcredit can help households cope with incidental setbacks as well (caused by illness, failed crops or accidents, for example).

The basic idea is that borrowers can and will invest the money productively, and therefore achieve a higher return than the interest on the loan (often 15% to 25% or even higher).[20] Collective responsibility for the loan could be one way of keeping the interest relatively 'low'. The social pressure in such a case would be high.

Another characteristic of microfinance is a strong focus on women (Duvendack et al., 2011). Women belong more frequently to the poorest groups and appear to be more reliable when it comes to paying back loans (Bauchet et al., 2011). Women also appear to achieve better results than men (Pitt and Khandker, 1998; Dupas and Robinson, 2012), though some studies cite better results for men (McKenzie, 2009). Women usually have less access to the

[19] IEG gives an impact score of 71% to microfinance institutions, and 61% to projects for banks that serve SMEs, which is equal to the average IFC score for these countries.

[20] NGOs usually ask for higher interest rates than banks (see Cull et al., 2009).

labour market, so becoming a self-employed entrepreneur is a potential solution for some (Karlan and Morduch, 2010).

Following the initial euphoria and positive outcomes (Pitt and Khandker, 1998; Khandker, 2005; Goldberg, 2005), recent studies have been more critical (Bauchet et al., 2011).[21] These studies are mainly rigorous impact studies, especially randomised controlled trials (RCTs) (see, for example, Banerjee and Duflo, 2011; Banerjee et al., 2013; Crépon et al., 2011; Fafchamps et al., 2011; Karlan and Zinman, 2011; ADB, 2012).[22] These studies paint the following picture:

- A small minority of borrowers use the financing to start their own company;
- Most households do not have the opportunity to start an activity (or expand one) that will yield a return of at least 24% (the interest rate). For those who borrow money, microcredit will at most allow them to temporarily escape poverty;
- In most cases, the company's profits do not increase (though that is the case with 'larger' micro-businesses), nor does consumption, an indicator of prosperity;
- Nor is there much, if any, impact on spending on education and health care; and
- Microcredit does affect the structure of consumption: loans make it possible to invest in sustainable consumption goods.

Various reviews have determined that despite apparent success there is no clear evidence that microcredit has a positive impact (see, for example, Sebstad and Chen, 1996; Gaile and Foster, 1996; Armendáriz de Aghion and Morduch, 2010; Duvendack et al., 2011; Copestake and Williams, 2011).[23] Too often, the evidence is based on anecdote, and more rigorous scientific research is unable to show any significant impact (Westover, 2008). Based on micro-economic research, which uses an international survey among households, Aggarwal et al. (2012) conclude that many studies overestimate the positive impact of microcredit. It also appears that the poorest groups rarely benefit from microcredit (ADB, 2012). There is even a realistic risk that microcredit has a negative effect on the poorest groups (Hulme and Mosley, 1996; Stewart, et al., 2010; Stewart et al., 2012; Shimamura and Lastarria-Cornhiel, 2010; Roodman, 2012): they could be inclined to use the loans for consumption instead of investment. Even if the loans are used for investment, then the return might be too low to pay off the high interest rates (15% to 25% or higher).

[21] Roodman and Murdoch (2009) and Roodman (2012) contested Pitt and Khander's findings, which led to a harsh polemic between the researchers.

[22] This approach works with a control group and completely randomly selected allocation of households to the intervention group or control group. This makes it possible to avoid potential selection bias. Selection bias occurs, for example, when microcredit primarily attracts people who wanted to start their own business anyway, for example (and probably would have anyway).

[23] The reviews by Goldberg (2005) and Odell (2010) are somewhat more positive. Odell emphasises that negative reports in the press should be greeted with some scepticism and that the studies mentioned also highlight positive effects. She also argues that the various instruments are too heterogeneous to be lumped together. On the other hand, the most robust studies (such as Banerjee et al. (2013)) and reviews (such as Duvendack et al. (2011)) are the most assertive in rejecting claims of microcredit's positive impact.

Stewart et al. (2010) conclude that focusing on microcredit for poor households is ill-advised, and that these programmes would be better off focusing on loans for businesses, instead of viewing everyone as an entrepreneur. The poorest people live by definition in a fragile environment, in which microcredit can only bring about limited change (see also Karlan and Morduch, 2010). It seems that the most important impact of microcredit – taking into consideration the previous point – is stabilising income (see also Rosenberg, 2010). Empirical research also shows that it is not so much loans to households that contribute to economic growth but better access to loans by businesses (Beck et al., 2011). Donations (in the amounts of US$ 100 to US$ 200) to poor households can be an effective way of improving incomes (McKenzie & Woodruff, 2012). But there is little point in providing small businesses with funds if there is no good preparation or supervision, or in the absence of a good entrepreneurial climate (ADB, 2012). According to development banks, financial education, consumer protection and accountability to customers has received too little attention until now.

The World Bank (2013) concludes that to only offer microfinance is not enough to entice investment and growth. The target group is heterogeneous, has a fluctuating growth potential, usually does not possess sufficient management skills and faces regulatory bottlenecks. Microcredit is not by definition the right instrument either, because the requirements for repayment (immediately after the loan has been granted) and the collective responsibility for the loan prevents risk taking. The World Bank concludes that training in the area of financial management could have a positive impact. However, it does not seem as if the extent of this impact would be huge. The various studies show, depending on the context, mixed outcomes.

Various studies show that micro-saving has a greater positive impact (the saving of small amounts by households and micro-businesses). Dupas and Robinson (2012) discovered a substantial impact among female market sellers: many women took advantage of the possibility to save. Four to six months after opening a savings account, these women had an average of 45% higher investments than the control group. The positive impact is reflected in higher private expenditures, according to the researchers. Bruné et al. (2011) found a similar impact among farmers in Malawi. Stewart et al. (2010; 2012) conclude, however, based on a systematic review, that there is little evidence for the contention that microcredit or micro-saving has a positive impact on economic opportunities for the poorest groups. Microcredit and micro-saving have the potential to reduce poverty, but not in all circumstances and not for everyone. It is therefore important not to view financing as an isolated activity.

3.3 Market development

Market development and trade

Poorly functioning markets can stifle economic development. Moreover, the relationship between local markets and (international) trade is complex. Comparative studies show that countries with more trade achieve higher economic growth rates in the long run, though the causality could just as easily be the reverse (Krueger, 1997). The literature cites four ways in which trade can contribute to economic growth (Rodrik, 1995):

1. Countries can focus on activities in which they have a comparative advantage;
2. Trade encourages technological development;
3. Trade weakens the impact of external shocks; and
4. Trade limits internal price distortions.

What is important in that respect is the knowledge that trade can only contribute to economic growth if the local entrepreneurial climate gives companies sufficient room for manoeuvre (Freund and Bolaky, 2008). Geographic location and the availability of raw materials, moreover, strongly influence the type of trade activity.

The continued impact of market development on the generation of employment and income depends heavily on the way in which trade relations are organised. Donors using the Aid for Trade (AfT) approach are devoting increasing attention to this through a broad range of programmes and projects. The recent OECD-WTO report, '*Aid for Trade at a Glance 2013: Connecting to Value Chains*' (2013) contains a detailed analysis of AfT developments worldwide and examines the findings of empirical studies and (impact) assessments of AfT projects by donors and the AfT policy in developing countries.[24] The report reveals that AfT programmes work best in low- and lower middle-income countries if they focus explicitly on reducing trading costs. Ways of achieving that include improving the economic infrastructure, facilitating trade, strengthening trade-related institutions (such as customs, standards bodies and organisations that promote export) and a trade policy that promotes competition. In addition to that, there remains the need for complementary policies in developing countries in order to reduce the negative impact of trade adjustment or growth. Ravallion (2004) shows in an overview study that poor households only benefit marginally from increased trade as a result of domestic price distortions. Trade liberalisation only leads to poverty reduction if there are complementary reforms that focus on deepening financial services, infrastructure improving good governance.

A recent study concludes that as an intervention in trade-related capacity building AfT should be integrated in the development of other sectors, including the social sectors (ICTSD, 2013). In line with the Paris Declaration's general lessons about aid effectiveness, Aid for Trade is at its most effective, according to ICTSD, when the developing country has built up its own capacity, the programme has broad political support and donor objectives are aligned with those of the recipient. Often, these conditions for success are still absent locally. ICTSD advises donors to first focus on that, instead of improving isolated AfT projects.

[24] www.wto.org/english/res_e/booksp_e/aid4trade13_e.pdf

Bottlenecks
Poorly functioning markets can stifle the development of (international) trade and ensure that various groups are unable to sufficiently benefit from the opportunities provided by trade. The literature cites two bottlenecks: (1) limited access to input or output markets and (2) weak or unbalanced competition in goods and services markets. Poor access to markets impedes the development of a balanced private sector. There are several potential causes for this:

- Entrepreneurs have difficulty accessing the market because of poor infrastructure or because of the poor quality of the infrastructure, which results in high (prohibitive) transport costs;
- Entrepreneurs have insufficient access to information about markets; and
- The dissemination of information about new production methods and techniques is flawed and sluggish, in part because public information services do not function well.

High transaction costs, market risks and limited information are important reasons why poorer small-scale producers in particular have poor access to markets (SDC/DFID, 2008). Bottlenecks arising from the structure and the functioning of markets in developing countries include:

- A lack of networks between producers, traders and the manufacturing industry that lead to high costs related to trade transactions between businesses;
- Small-scale producers are unable to bring sufficient volume to the market and are consequently at the mercy of middlemen;
- A lack of knowledge and information about prevailing market conditions; this concerns both the prices and the quality requirements that prevail in national and international markets;
- Monopolisation: a limited number of commercial market players that determine prices among themselves and prevent new players from joining;
- Trade barriers and limited interaction with the global market distort domestic price ratios; and
- Limited integration between local, regional and national markets, which causes massive price fluctuations and disproportionate margins.

McCulloch et al. (2002) distinguish between the direct and indirect impact of market development on three levels: (a) changes in prices within the market channel, (b) adjustments to wages, profits and employment at the business level, and (c) the impact of taxes and transfers on the relationship with the government. Improving access to market information (by means of mobile phones, for example) and to systems aimed at making trade transactions more efficient (such as warehouse receipts) can help to reduce risk and increase trade. Individual characteristics (level of education, social networks, age and gender) and contextual factors (such as investment climate, customs requirements, macro-economic stability) determine to a large degree how effectively one can participate in trade.

'Making markets work for the poor' (M4P) programmes strengthen the links between market players at the levels of client networks, knowledge exchange and incentives. In that respect, improving market access often requires an integrated approach, in which programmes that work to strengthen the input side of the market are used in tandem with investments in physical infrastructure and in the financial sector, by spreading knowledge and information and by adapting laws and regulations. Investments that contribute directly to improving the functioning of markets focus on the quality of production processes, cooperation between market players and access to international markets. An increase in (the value of) sales is the most important performance indicator in that respect.

In this approach, the functioning of the market systems and value chains is increasingly viewed as the main factor that determines the net impact for poorer households. Market development can help to strengthen trade and hence incomes as well, providing the players in the chain work together with lead firms, such as food processing multinationals and supermarkets, in areas such as knowledge exchange, risk and cost sharing, co-investment in product or process improvement (upgrading) and transparent chain management. This could include several different types of intervention (Humphrey and Navas-Alemán, 2010):

- Interventions that strengthen the weakest link. For example, a common problem in the manufacturing industry is the poor quality of the raw materials. As a result, costs are higher and the quality of the end product is sub-par. Interventions aimed at improving quality benefit the entire chain;
- Information exchange and market research: knowledge and production means are rarely shared between businesses in a chain. Businesses are often unaware of what their customers want, especially when they are far removed from their customers;
- Improving connections between different links (relationships between producers) in the chain, for example by means of quality labels and certification; and
- Developing alternative relationships in a chain (alternative supply and sales markets).

Research results

Studies in the past have harshly criticised the effectiveness of organisations in developing countries that focus on promoting export. Export promotion activities were not effective as a result of bureaucratic structures, mismanagement, customer-unfriendliness and a lack of resources (Hogan et al., 2001). A great deal has changed, partly in response to these criticisms. Various researchers discovered that promoting export was having a positive impact recently (Lederman et al., 2005; Volpe, 2010a; 2010b; Volpe and Carballo, 2010). Export promotion activities are mainly effective when it concerns entering new markets (countries) or exporting new products.[25] That is much less the case for existing markets and products. Volpe and Carballo (2010a) conclude that export promotion activities are potentially important primarily for promoting a more diversified export structure. It also appears that small businesses benefit more from these activities than large enterprises.

25 Volpe and Carballo (2010) did not discover an impact in Uruguay for new exports to OECD countries.

Experiences with programmes that focus on value chains are mixed, despite the logic behind them. Donovan and Poole (2013) discovered that not all households involved in a project in Nigeria were able to profit from the strengthening of the cooperation that was set up there. One of the reasons was that the project did not invest in knowledge, as a result of which the participating farmers used the wrong seeds or applied the fertilizer incorrectly. The poorest farmers were not in a position to invest either. In theory, small interventions in a value chain should yield major development benefits. In practice, however, there are many limiting factors, such as poor quality of infrastructure, and governments and donors who devote little attention to the sector. Another example concerns setting up value chains for farmers in Kenya who produce for local supermarkets (Rao & Qaim, 2013). Research also shows that the impact is not the same for everyone. Better educated farmers turn out to be more innovative, are quicker to use modern marketing techniques and therefore have more chance of actually supplying supermarkets. Moreover, farmers who are employed (elsewhere) have more chance of participating in the project, probably because they can invest more easily as a result of income earned outside of their farms. Access to transport is also extremely important.

Both examples show that while the theory asks for a more holistic approach, projects do not always comply. In such cases, a project may help wealthier farmers, while the poorest farmers barely benefit. A mistake that is made in various interventions is that projects assume that poor households possess the right characteristics to jointly benefit, and that partial strengthening is sufficient to raise them out of the poverty trap (Stoian et al., 2012). The interventions assume that poor people have sufficient resources to participate, and that they can take the risk of using all resources on that one product (or channel). An equally important conclusion is that the ultimately envisaged impact of projects are rarely examined (Humphrey and Navas-Alemán, 2010; Stoian et al., 2012).

3.4 Knowledge and skills

Bottlenecks

According to mainstream (neoclassical) economic literature, developing countries should be able to slowly but surely catch up with prosperous countries (Barro & Sala-i-Martin, 2003). There are several reasons for this contention, according to the theory: declining marginal capital returns and the possibility to imitate production methods and technologies from affluent countries. The reality is more complex than that, however, and for decades many countries in the South had lower growth rates, and ultimately the gap between rich and poor only widened. One of the explanations is low productivity (Bloom, Mahajan, McKenzie and Roberts, 2010) (McKenzie and Woodruff, 2012). For example, at the end of last century, labour productivity in South Africa was only 20% of what was in the United States (Van Dijk, 2003). The situation has changed since then, however. In the early 2000s, labour productivity began to grow at an average of 2.7% in Africa (McKenzie and

Woodruff, 2012). Nevertheless, Harrison et al. (2013) found that labour productivity in sub-Saharan Africa was on average 36% lower than in other countries.[26]

Low labour productivity is connected to employment patterns. A large part of the jobs in developing countries are concentrated in small businesses that are not particularly dynamic (World Bank, 2012b). It often concerns smallholder agriculture or employment in informal services. Despite being important for overall employment, their contribution to growth and productivity improvement is very limited (World Bank, 2012b). The businesses create jobs, but they are just as easily lost again (Sonobe et al., 2012). Well-run enterprises, on the other hand, are innovative and enjoy high growth in terms of productivity and employment.

One of the causes of low productivity is an inadequate level of knowledge. Good education remains, despite advances in recent decades, a major bottleneck. Governments and donors have focused mainly on improving primary education, but have neglected to devote attention to higher education. Vocational education is out of date, and the skills that pupils learn are no longer aligned with the demands of modern businesses. Because vocational education has a bad reputation, pupils only opt for it if there is no other alternative.

It is not only about the employees' skills but just as much about the skills of entrepreneurs and management (see, for example, Bartelsman et al., 2009; Hsieh and Klenow, 2009; Sonobe et al., 2012). According to the World Bank (World Bank, 2012b), an increasing flow of publications is emphasising the importance of management skills for productivity improvement. Differences in productivity between businesses can largely be explained by differences in knowledge and skills between entrepreneurs. Small self-employed entrepreneurs usually lack basic management skills (Sonobe et al., 2012). They do not see the point of investing in management training (Mano, et al., 2011; Bloom et al., 2013). It turns out that after having had training entrepreneurs are prepared to pay for follow-up training, and other entrepreneurs who see the results are also willing to pay for training (Sonobe et al., 2012).

These problems are not limited to micro-businesses. The lack of management skills in larger businesses is an important cause of limited or stagnating growth (Bloom and Van Reenen, 2010). The absence of marketing and the lack of concrete (financial) goals, quality control and management of the activities impede growth and productivity (McKenzie and Woodruff, 2012). Bloom et al. (2013) cite India as an example, where the absence of quality control systems means that problems selling products persist for a long time. Weak management is also evident in the mixing up of private and business expenditures, as well as rudimentary or even wholly absent systems of administration.

26 The authors compared countries in sub-Saharan Africa with countries outside Africa with an average annual income of less than US$ 3,000 (based on purchasing power parity) . The conclusion applies to the best 50% of this group.

A culture also exists in which middle management has no incentive to develop new skills, and management does not put the means at people's disposal in the first place. Decision making is so dominated by the amount of time available at the top that a bottleneck arises that keeps the business from growing (Bloom and Van Reenen, 2010). Centralism prevents effective and timely decision making at the right level, and as a result actual productivity improvements lag far behind their potential.

Interventions

Governments and donors have spent many hundreds of millions of euros in recent decades on measures aimed at improving businesses' productivity, sometimes referring to these measures as 'business development services'. These measures concern a huge variety of non-financial activities aimed at access to means of production, survival, productivity, ability to compete, and the growth of small and medium enterprises. The available services include: training, advisory services, help with marketing, information services, technological development and promoting value chains (see IADB, 2003). Training programmes focus on entrepreneurship, for example, as well as planning and marketing, production and quality management, administration, cost projection and management, quality control, stock management and human resource management (Mano et al., 2011; Bloom et al., 2013; Sonobe et al., 2012). Other projects focus on providing targeted advice (Bruhn et al., 2012).

Another way of promoting the transfer of knowledge and technology is to encourage joint ventures, i.e. partnerships between Western companies with businesses in developing countries. These joint ventures could benefit both parties (Miller et al., 1996; Ahiaga-Dagbui et al., 2013). Local businesses offer foreign investors the advantage of having knowledge of local markets, politics and regulations, as well as their local reputation. The benefit for the local partner is often access to technology, the foreign investors' international reputation, financing and management know-how. There are disadvantages as well. Research shows that joint ventures are often difficult to manage, in part because of cultural, legal and political differences (Huang, 2003). According to Beamish and Berdrow (2003), more than half of all international joint ventures with businesses in developing countries fail.

In addition to advisory services, training and encouraging the development of international joint ventures, more attention has been devoted to supporting producer organisations in recent years, especially farmers. Many of the poorest people in developing countries live in rural areas. They are often smallholder farmers, who consume part of their production themselves. Africa's recent history shows that it is precisely this group that has barely benefited from economic growth in other sectors. For them, transaction costs are high, and they also have weak bargaining positions in markets. Usually the farmers only have limited access to financial and public services, and they rarely have a voice in political forums (World Bank, 2007). Since the 1980s, many farmers have set up producer organisations with the aim of strengthening their market position, increasing their political influence and therefore also gaining better access to public services. In 2007, the World Bank estimated that 250 million farmers were members of a producer organisation. The organisations have three main functions (Cook and Chaddad, 2004):

1. Expanding their markets;
2. Improving access to and quality of services (including credit, technical assistance and marketing); and
3. Increasing the participation of both male and female farmers in political decision-making processes.

The focus in developing countries is often on the first two external functions. The third function usually receives less attention, especially in countries where the government set up (public) cooperations in the past.

Producer organisations are nothing new; indeed, they have existed for a long time in developing countries. The Netherlands has, especially in the agricultural sector, a long tradition of cooperative organisations. This knowledge and experience has been used in several international cooperation programmes. According to the *World Development Report 2008* (World Bank, 2007; see also Ton et al., 2007), donor organisations can play an important part in strengthening the capacity of producer organisations by:

- Supporting the management of these organisations (financially, and with advisory services and training);
- Technical assistance in the areas of market information, production, procurement and distribution, and plant health and quality standards; and
- Advisory services in the areas of policy analysis and negotiations.

The effectiveness of these kinds of cooperative efforts depends strongly on the degree to which the programmes are actually demand driven.

Research results

We still know little about the impact of programmes that focus on improving knowledge and skills in businesses. In the first place, this is because few projects are being evaluated in a scientifically responsible manner (McKenzie and Woodruff, 2012). The evaluation service of the Inter-American Development Bank (IADB, 2003) concludes that many projects lack a clear focus and objectives: interventions and target groups are not clearly defined or chosen based on the anticipated benefits. It was barely possible to evaluate projects, nor did researchers find any evidence of effectiveness. Evaluations often focus on the implementation process, as if successful implementation equates sustainable impact. When impact studies are conducted, then the sample survey is often too small to make robust conclusions.[27] Another bottleneck is that an assessment of the (sustainable) impact is only possible after a number of years.

[27] Although various studies focus on as many as 100 to 300 businesses, their statistical value – which is an important gauge for the degree to which the discovered links can be generalised – is weak because of the huge differences among them.

The research results painted a varying picture. Businesses involved in a project with textile mills in India achieved an increase in productivity of 17% following targeted training lasting four months (Bloom et al., 2013). Bruhn et al. (2012) discovered an 80% rise in sales and a 120% increase in productivity following advisory services (provided by local consultants) to participants in a project for small enterprises in Mexico. The resulting benefits were primarily the consequence of improved marketing and better financial control. For that matter, only 80 of the 150 selected businesses actually bought the advisory services, which points to the existence of self-selection (the subsidised services were bought by entrepreneurs who expected the greatest advantage from the services) and therefore also overestimation of the training's impact. Researchers did not find any significant impact of management training for entrepreneurs from SMEs on their business results in Ghana (Mano et al., 2011). An important explanation for this is that approximately half of the entrepreneurs did not follow the advice they were given. A project in Sri Lanka studied the impact of training programmes on female entrepreneurs (De Mel et al., 2012). The evaluation shows that women did put to use several of the skills they learned from training, but these skills did not influence profit or turnover. A group of potential entrepreneurs did initially benefit from both the training and the combination of training with a financial contribution: they were quicker to set up a business and were more successful after two years. The researchers conclude from this that training is especially effective with start-ups, a conclusion that does of course depend heavily on the nature and content of the programme. Sonobe et al. (2012) conclude – based on experiments in Vietnam, Ghana and Tanzania – that management training helps to improve a number of basic skills. This decreases the chance that entrepreneurs – whether forced to or not – have to shut down their businesses (see also Mano et al., 2011).

Based on a review of literature, the World Bank (2012) concludes that evaluations of training programmes show that they are effective in terms of entrepreneurs' financial literacy' and management skills. The impact on businesses' results (in terms of turnover and profit), as well as employment opportunities, are also positive, but less robust. According to the organisation, there is sufficient evidence that the benefits outweigh the costs. Much of this 'evidence' is based on research from developed countries though (see also Sluis et al., 2005). The experiences with several experiments, however, leave a number of questions unanswered. It is not clear with which type of business or entrepreneurial background that management training is most effective (IADB, 2003; Sonobe et al., 2012). In addition, the precise information need is not always clear either. Several basic patterns do emerge from the literature, however:

- Training programmes can be especially effective for start-up businesses (De Mel et al., 2012);
- The best results are achieved by entrepreneurs who already had better skills when training started and also more access to financial resources; and
- Training can succeed if it is kept simple, if the right training materials are available, and if the training also lasts long enough and the entrepreneurs involved in the training are sufficiently motivated (IADB, 2003; Mano et al., 2012b).

Sonobe et al. (2012) conclude that while providing basic skills is important, it is not enough for the dynamic growth of a business. For that to occur, innovative capacity is needed – and that is much more difficult to learn. Experience working in larger, more productive businesses is possibly more useful than following a training programme (World Bank, 2012b). Indeed, there is little point in management training if the investment climate is unfavourable.

There is not much empirical evidence yet either pointing to the effectiveness of producer organisations or their support (Bernard & Spielman, 2009) (Ragasa, 2012). The research mainly concerns case studies, the outcomes of which are not unequivocal. A great deal depends on the specific context in which producer organisations operate. For example, to achieve economies of scale in buying inputs or selling end products, the impact depends heavily on prevailing market conditions and the nature of the product. Fresh produce (vegetables, fruit, fish and milk) benefits from short chains and strong quality control. The advantages for those who supply supermarkets or multinationals are essentially limited to medium-large producers. Smaller producers often enjoy advantages in the areas of knowledge dissemination and better inputs. These impacts are usually temporary in nature and spread themselves quickly across larger groups of producers. Ragasa (2012) and Golan (2012) conclude that the effectiveness of rural producer organisations depends on a favourable environment, good governance and safety. The authors also attach great importance to interaction with external actors, who can provide information, technical support, and access to markets and services. Involvement of the members is also a condition for an effective organisation. Management and organisation training can help increase the effectiveness of weak organisations.

3.5 Laws and regulations

Laws and regulations and economic growth

Opinions vary in international economic and political literature on the importance of institutions and law and regulations. Authors such as North (1990; 2009) and Acemoglu and Robinson (2012) argue that economic and political institutions determine a country's economic development. In doing so, they also explain why some countries, or more accurately the political elite in some countries, can cling so tenaciously to faulty institutions. There are other opinions on the matter too, however. Chang has argued in several publications (2002; 2007; 2010) that it is not institutions that influence economic growth but, on the contrary, it is economic development that determines the shape institutions take on. According to Khan (2011), fast-growing and slow-growing developing countries have very similar indicators in the area of good governance (including laws and regulations for the business sector; see also Dijkstra, 2013).

In the late 1980s, Hernando de Soto pointed out the enormous bureaucratic obstacles that starting entrepreneurs faced in Peru when setting up their business.[28] As a result, many small entrepreneurs that remained in the informal sector were unable to fulfil their potential (De Soto, 1989). Indeed, there are indications that abolishing the unnecessary, expensive and time-consuming rules for starting a business clearly has a positive effect on the number of officially registered enterprises. The effect, however, is not so great and disappears in the course of time. Some studies point to an increase of about 5% in the period after the jungle of rules and procedures was replaced by a one-stop-shop for registering businesses (Motta et al., 2010). In most cases, it concerned new start-up businesses and not informal companies that had now decided to officially register.

It appears that informal businesses often choose to operate in the informal sector because formalisation presents more disadvantages than advantages (McKenzie, 2009). A recent impact assessment in Bangladesh discovered that reducing the registration procedure to one day – instead of 42 days – in combination with an information campaign about it had no impact on the registration of informal businesses (De Giorgi and Rahman, 2013). The indirect costs for formalisation – such as paying taxes and meeting product requirements and labour standards – prevented these businesses from officially registering. An experiment in Sri Lanka confirmed that the size of a business and its prospects determine whether or not a business will decide to register when rules and procedures are relaxed (De Mel et al., 2012). The fact many choose to start their own (informal) business for want of better alternatives is an important factor in this (World Bank, 2012b).

Relaxing the broad range of government regulations for businesses became the focus of the World Bank's influential *Doing Business* approach. The World Bank encouraged, advised and supported governments financially as they implemented reforms. From 2003 onwards, the organisation published a list of countries ranked according to the 'ease of doing business'. The World Bank evaluated countries on ten aspects related to the policy environment of businesses: procedures for starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting investors, paying taxes, import and export procedures, enforcing contracts and resolving insolvency. In the past ten years, *Doing Business* has registered almost 2,000 reforms of laws and regulations in 180 countries. Singapore is ranked first in the 2013 *Doing Business* report, the Central African Republic last (185th) and then Netherlands 31st (World Bank and IFC, 2013).

There is a great deal of debate about the value of the *Doing Business* (DB) indicators. Recent research confirms the assumptions behind the *Doing Business* project. According to Haidar (2012), there is a long-term connection between the number of reforms in the areas of doing business and economic growth: every reform that a country carries out goes hand in hand with an increase of 0.15% of GDP. The relaxation of import and export procedures is a particularly strong economic incentive. This is in line with earlier findings that in

[28] In Peru, 11 permits were needed to register a business, which took an average of 289 days and cost more than US$ 1,000.

Africa every extra day of delay in transport reduces trade volume by 1% and thus impedes economic development (Djankov et al., 2010). Research on the predictive value of the *Doing Business* rankings also identified the indicator for trade barriers as a criterion with little distinguishing power (Høyland et al., 2009).

Others are more critical of the indicators. A study that compared the outcomes of 40,000 of the World Bank's business surveys in almost a hundred countries with the *Doing Business* indicators observed a substantial difference between the formal rules and what businesses actually experienced (Hallward-Driemeier and Pritchett, 2011). Many businesses discovered more flexible circumstances than the official rules would have led them to expect. Corruption and favouritism may have played a part in this. A Norwegian study concluded that it would be easier for developing countries to improve their ranking on the list than it would be for them to actually carry out improvements in their entrepreneurial climate (Høyland et al., 2009).

In 2008, the World Bank's evaluation service (IEG) judged the DB concept to have been successful in promoting reforms in laws and regulations for businesses (Independent Evaluation Group, 2008). At the same time, IEG criticised the relevance of the DB country list: laws and regulations only encompass a fraction of the factors that have an impact on investment decisions by businesses. Other factors, such as access to affordable credit and a good electricity supply often have a greater effect on businesses' growth opportunities (Dinh et al., 2010). And sometimes more rules were needed, not fewer – for example, to prevent child labour and exploitation (see also Chang H., 2010). On the other hand, reinforcing property rights can improve access to credit (World Bank, 2013).

Land rights

Registering land rights is a specific aspect of law and regulation reform. For the Netherlands, this was an important issue in its development policy, from the perspective of private sector development as well as food security and strengthening the position of women. In recent years, this issue has become even more topical as a result of the debate on land grabbing (the large-scale purchase of land by foreign investors or speculators, especially in Africa).

Determining land rights could lead to more productive investments, according to the theory, because owners would have the certainty of being able to benefit from their investments for a longer period of time. Access to credit could also improve, because the land would now serve as collateral for a loan (De Soto, 2000). Determining land rights could also improve the marketability, leasing and optimal allocation of land.

Studies confirm the positive impact that the granting of land rights have on investments and on productivity in many Asian, Latin American, East European and African countries (Deininger, Ayalew Ali and Alemu, 2008). Researchers conducting a multi-year study on the impact of issuing land certificates in the Tigray region of Ethiopia found that there was better soil maintenance, higher productivity (+45%) and more investments in trees (Holden, Deininger and Ghebru, 2009). The issuing of formal property rights in Peru also led to greater willingness to invest, especially with farmers who previously had the most uncertain land rights (Fort, 2007).

The relationship between land rights and access to credit turned out to be much weaker in practice than expected, and was even absent in some cases (Deininger, et al., 2008). For farmers with the smallest farms in Peru, registering their land was insufficient for collateral for a loan. Farmers who owned somewhat more land often baulked because of the risk of losing the land if they could not repay the loan on time (due to crop failure, for example). Only farmers with a lot of land and often a higher education dared to take the risk and used their land as collateral (Fort, 2007).

4

Dutch private sector development policy: activities and results

4.1 Dutch policy promoting private sector development

Private sector development (PSD) became an increasingly central focus of Dutch development policy during the evaluation period 2005-2012, especially from 2010 onwards. This coincided with a shift in focus in Dutch aid from social development to economic development.

While the PSD policy during the evaluation period remained focused on economic growth and poverty reduction, successive ministers emphasised different aspects of this policy area. During the period 2003-2007, these ministers supported the approach in developing countries to remove specific bottlenecks in the business climate and encourage local entrepreneurship, all of which involved a key role for Dutch embassies. Moreover, new partnerships were initiated with Dutch businesses and social enterprises, based on their expertise in specific fields, such as horticulture and water.

Growth and distribution became one of the four spearheads of development policy in the years 2007-2010, and private sector development was an important part of it. The Netherlands wanted to use a number of (largely already existing) activities to create a better entrepreneurial climate. The minister at the time developed new partnerships with parties in the business sector. He also focused on developing the agricultural sector.

From 2010 onwards, private sector development was one of the core businesses of Dutch development policy, and a key principle was the involvement of the Dutch business sector. Indeed, the knowledge and skills of the Dutch 'top' sectors had to be put to optimal use. Food security became an important theme. New public-private partnerships were set up, with a focus on food security, for example. A new fund was established to support Dutch SMEs investing in developing countries. Corporate social responsibility became a condition for companies to participate in the programmes. While the list of bilateral partner countries was drastically reduced to 15, the business sector instrument was made available to 66 countries. The support explicitly set out to create mutually profitable trade and investment relations, especially with developing countries that had managed to escape the worst poverty.[29] The Netherlands went in search of new combinations of aid, trade and investment. The appointment in 2012 of a minister for foreign trade and development cooperation meant that for the first time the two objectives of poverty reduction and economic interest were married in the same ministerial portfolio.

4.2 Intervention logic and expenditures

The above information has enabled IOB to produce a results chain for PSD policy (see table 1). The results chain shows that PSD policy focused on improving the entrepreneurial climate in the broader sense. It worked according to the five clusters, and within each cluster there were a number of specific objectives at the output and outcome levels.

[29] The actual link between bilateral aid and the Dutch supply of goods and services had been gradually abandoned in favour of an independent bilateral development policy. International agreements at the OECD level about disciplining export support and untying aid to the least developed countries (LDCs) reinforced this change and were partly achieved on the initiative of the Netherlands.

Table 1 Results chain for PSD policy (2005-2012)

Input Ministry of Foreign Affairs	Channels	Thematic focus (5 clusters)	Most important instruments / programmes	Most important activities
	Bilateral	Infrastructure (EUR 1,171 million)	ORET FMO-IDF PIDG ORIO	Co-financing local infrastructure Supplying (Dutch) capital goods and technology
Financial Recources (ODA)		Financial sector (EUR 736 million)	FMO-MASSIF NIPP GTLP FMO-CD TCX	Financing and supporting broader service provision for financial intermediaries Developing innovative financial products
Human recources (FTE)	Businesses and NGOs	Market development (EUR 550 million)	CBI IDH Solidaridad IFDC	Advising on products and product processes Setting up partnerships for more sustainable market chains
		Knowledge and skills (EUR 615 million)	PSOM/PSI PUM Agriterra Woord en Daad	Co-financing joint ventures with NL businesses Analysing business operations Financing/setting up vocational education
	Multilateral	Laws and regulations (EUR 60 million)	Bilateral programmes in Bolivia, Rwanda, Zambia etc. ICF-Afrika	Analysing bottlenecks in entrepreneurial climate Advising and providing technical assistance to governments (incl. on land governance)

<table>
<tr><th>Output</th><th>Outcome</th><th colspan="2" rowspan="2">Impact</th></tr>
<tr><th colspan="2">‘better entrepreneurial climate’</th></tr>
<tr><td>Roads, bridges, ports, electricity, hospitals, water and sanitation, irrigation, telecom, etc.</td><td>Better access and use of infrastructure

Lower transaction costs for businesses</td><td rowspan="5">Higher investments (national + FDI)

More viable businesses

Better paid jobs

Growth in productivity

Better operating results

Larger formal economy</td><td rowspan="5">ECONOMIC GROWTH & POVERTY REDUCTION</td></tr>
<tr><td>Larger, better and greater variety of financial services

New financial products

Reforming financial system and national monitoring</td><td>Better access and use of (innovative) financial services, especially by SMEs, poorer groups and women, and in rural areas</td></tr>
<tr><td>Advice and reports about production and product processes

Partnerships in market chains</td><td>Better quality of production and production processes

Increased sales for businesses at in national, regional and international markets</td></tr>
<tr><td>Joint ventures

Advisory service for businesses

Trained entrepreneurs and employees

Better organised producer organisations</td><td>Production innovation

Better business operations and stronger entrepreneurship

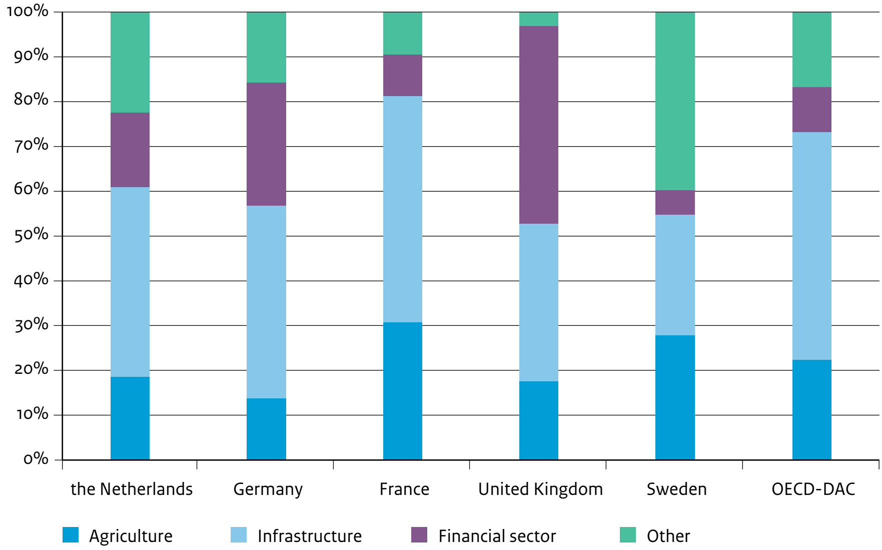
More robust social dialogue</td></tr>
<tr><td>Reports, proposals, seminars, etc. aimed at reforming laws and regulations</td><td>Reforming of laws and regulations (indicator: Doing Business score)</td></tr>
</table>

Source: reconstructed by IOB.

Dutch PSD expenditures

The Netherlands' spending pattern is generally similar to that of other donors in terms of the ratio between expenditures in the most important PSD sectors (see figure 2).

Figure 2 *PSD expenditures by the Netherlands by sector, compared to several other donors in the period 2005-2011 (incl. agriculture)*



Source: OECD, 2013.[30] Bilateral ODA (expenditures).

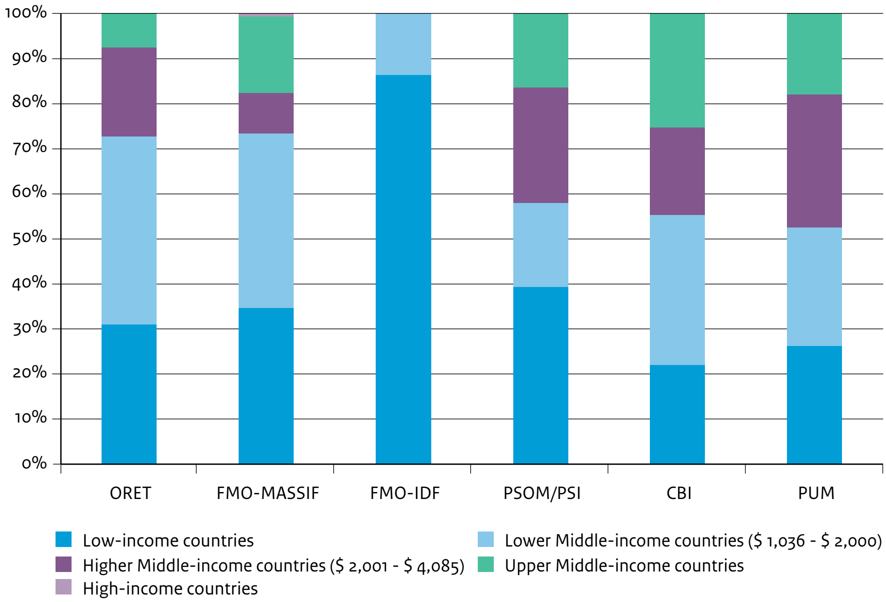
Between 2005 and 2012, developing countries received a total of more than EUR 3.3 billion in support for private sector development. That is more than 9% of overall Dutch aid in this period. In the period under evaluation, the percentage remained essentially equal. The heightened focus on PSD since 2010 has not led to an increase in expenditures on private sector development during the evaluated period. More than half of all expenditures went to six major programmes that were centrally run from the Netherlands. Two major infrastructure programmes combined received almost a third of the funds: the programme for Development-related Export Transactions (ORET, almost EUR 800 million) and the infrastructure fund for the least developed countries, managed by the Dutch Development Finance Institution (FMO-IDF, for the amount of almost EUR 200 million). The dominant player in financial sector development was MASSIF (EUR 280 million), a fund for SMEs in developing countries, which is also supervised by FMO. The amount of EUR 180 million went to the independent Centre for the Promotion of Imports from Developing Countries

30 IOB selected, for the computation of expenditures in the area of PSD, the following categories in the OECD Statistics Creditor Reporting System (http://stats.OECD.org/): Agriculture, Forestry, Fishing (CRS code 310 III.1), Transport and Storage (210 II.1), Communications (220 II.2), Energy (230 II.3), Banking and Financial Services (250 II.4), Business and other Services (250 II.5), Industry, Mining, Construction (320 III.2), Trade Policies and Regulations (331 III.3.a), Tourism (332 III.3.b).

(CBI). The Private Sector Investment Programme (PSOM/PSI) was also one of the most important expenditure categories with EUR 300 million. This programme provided subsidies to (Dutch) companies to encourage them to set up joint ventures with local enterprises. The ministry spent approximately 15% of the funds through diplomatic missions. PUM is the programme that outsources Dutch senior volunteer managers (EUR 70 million).

Ghana, Tanzania, India, Sri Lanka and Bangladesh belong to the group of countries with the most PSD projects. For the rest, a major part of expenditures went to (other) middle-income countries (figure 3).

Figure 3 *Spending by six central programmes by country income category (2005-2011)*



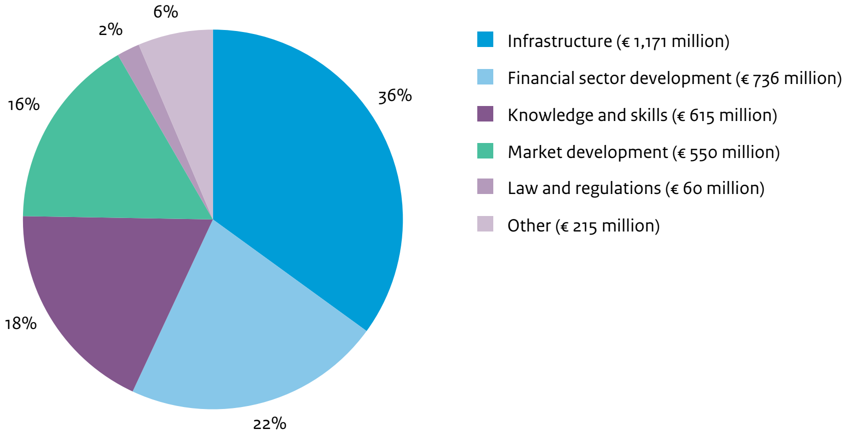
Source: IOB survey among programme administrators, 2013.

Approximately a quarter of all PSD resources were aimed at individual, selected companies, both of Dutch and other origin. The other PSD resources were to varying degrees meant to tackle bottlenecks in the general entrepreneurial climate or in specific sectors. The Netherlands used a significant part of the resources to extend credit opportunities for SMEs in developing countries. In addition, many of the resources were also used in the form of supplies from and assignments for Dutch businesses to improve infrastructure in developing countries.

4.3 Policy clusters: activities and results

The ministry organised the extensive set of instruments into a category of five clusters: infrastructure, financial sector development, market development, knowledge and skills, and laws and regulations. Figure 4 presents the distribution of expenditures among these policy clusters during the research period.

Figure 4 *Expenditures by thematic cluster in millions of euros and in percentages (2005-2012)*



Source: financial administration system Ministry of Foreign Affairs.

IOB examined how 32 instruments, divided into five clusters, were evaluated and what the conclusions are. Tables 2 and 3 summarise the results in terms of the degree to which the impact of these programmes were evaluated during the period 2005-2012. Table 2 does this on the basis of the number of programmes; table 3 does the same for the expenditures. The results show that most programmes were evaluated in one way or another. This is not surprising, because we are dealing with the largest programmes here. There is one major disclaimer, however: the largest programme (ORET) is precisely the one that was not, strictly speaking, evaluated during the review period.

Table 2 Number of activities and number of evaluated programmes (2005-2012)

	Number of activities	Evaluated programmes	Evaluated	Analysis of effectiveness		
				Extensive	Limited	None
Infrastructure*	45	6	6	3	0	3
Financial sector	84	8	8	1	4	3
Market integration	143	8	6	0	3	3
Knowledge and skills	110	4	4	1	1	2
Law and regulations	33	6	6	1	1	4
Other	301					
Total	**716**	**32**	**30**	**6**	**9**	**15**

* *Including ORET evaluations (2006).*

The most serious concern is the degree to which the evaluations focused on a systematic impact assessment: it was only the case to a (very) limited degree in 9 of the 30 evaluated programmes, and it was not the case at all in another 15 of the 30. Evaluations often report on the ability to reach beneficiaries or the implementation by beneficiaries (in this case the first recipient), but only rarely about the impact on the ultimate target groups, including specific consequences for women and the environment. Very few evaluations focused on the ultimate objectives in terms of improving incomes, reducing poverty and generating economic growth. When they did, it was usually not based on systematic (field) research. As a consequence, we actually know very little about the effectiveness of the various programmes. Based on the results, it is also almost impossible to indicate which priorities the ministry should set. In terms of the financial details, the picture is more favourable, which means the largest programmes underwent better evaluation.[31]

Table 3 Total expenditures and expenditures by evaluated programme (2005-2012)

	Number of activities	Evaluated programmes	Evaluated	Analysis of effectiveness		
				Extensive	Limited	None
Infrastructure*	1,171	1,058	1,058	971	0	87
Financial sector	736	616	616	10	243	363
Market integration	550	350	321	0	108	213
Knowledge and skills	615	455	455	304	9	142
Law and regulations	60	40	40	9	2	29
Other	215					
Total	**3,347**	**2,519**	**2,490**	**1,294**	**362**	**834**

** Including ORET evaluations (2006).*
Expenditures in EUR millions.

The lack of systematic evaluations in the area of private sector development is not a specifically Dutch problem. International programmes supported by the Netherlands generally do not undergo better evaluation. Other researchers also mention the lack of good evaluation in the field of PSD (see McKenzie, 2009; Spratt and Collins, 2012). Programmes for microfinance are a favourable exception. In terms of the target groups, these programmes are the most closely associated with the social sectors (programmes for education, health, and water and sanitation, for example), which generally undergo better evaluation.

31 This conclusion, however, depends heavily on the assessment of both ORET evaluations from 2006. The PSOM/PSI evaluation is to a large degree responsible for the positive result in the knowledge and skills cluster. However, this evaluation does not provide insight into the net impact or indirect impact: the report does devote a great deal of attention to the direct impact on employment, but not to the ripple effect or the potential loss of employment at other businesses.

Many of the reasons cited for the lack of systematic evaluation include:
- The development impact of PSD programmes are apparently difficult to measure;
- The various programmes and funds finance only part or a limited part of the projects; and
- The programmes and funds finance strongly heterogeneous activities.

There is no basic difference with social sectors on these points, however (see also McKenzie, 2009). The most important reason for the limited number of impact assessments in the area of PSD appears to be that the implementing organisations (and the ministry) have traditionally focused on financing and direct outputs and much less on the development impact (see also Spratt and Collins, 2012).

The results indicate the need to improve the situation. To make this happen, it is important that the programmes and future evaluations focus on:
- Carrying out baseline studies;
- Systematically collecting quantitative data at the impact level; and
- Carrying out evaluations at the programme level: the evaluations should not be limited to individual projects, but should rather focus on studying the added value of the programme as a whole.

Partly on the initiative of IOB, the ministry made agreements in 2012 with administrators of PSD programmes to improve evaluations, by developing an evaluation protocol, for example, and by freeing up resources for rigorous impact assessments.[32] This offers the hope that evaluations will produce more robust findings in the future. At the international level, the ministry has taken the initiative to increase the quality of Private Infrastructure Development Group evaluations. It is still too early, however, to be able to report on the results.

Infrastructure
The Netherlands has made significant contributions in recent years to the financing of infrastructure projects in developing countries. Between 2005 and 2013, the ministry supported investments in infrastructure to the tune of EUR 1.2 billion. A considerable part of that (67%) was earmarked for one programme (ORET). Poor infrastructure, especially in sub-Saharan Africa, is partly the result of years of neglect, both by governments and donors. At the moment, there is talk of true recovery. The Netherlands has set up various infrastructure funds and is also supporting several international funds.

Despite the extent of the resources, the various programmes were only evaluated to a limited degree. Most evaluations have the character of a review, whereby consultants primarily examined the management structure and investigated the degree to which outputs were actually achieved. Only on rare occasions did evaluations focus on the ultimate objectives of reducing poverty and generating economic growth. Evaluations

[32] The evaluation protocol is partly based on a standard set by the Donor Committee for Enterprise Development to provide more insight into the results and indicators of private sector development.

mainly identify reach and also often assume that the anticipated numbers will be achieved in the end as well. Reach is often considered the full responsibility of the financial institution in question, even though other funders will have contributed as well. In this line of reasoning, the assumed leverage effect (the catalytic impact) is the greatest if the contribution of the institution in question is minimal. That is a somewhat overly simplistic way of looking at the situation. If the fund gets involved in projects that it would have joined anyway, then the catalytic impact is zero. IOB's experience is that the catalytic function and additionality are often exaggerated (see box 1). The Netherlands, incidentally, is not an exception in that respect (WSP International Management Consulting, 2007). Spending pressure can result in a fund or programme financing a project that did not need it.

Box 1 *Additionality and catalytic impact*

The concepts of additionality and catalytic impact play a key role in many PSD programmes. The concepts form the argument and often the *conditio qua non* for financing. The development banks, after all, have to ensure that they do not encroach on commercial financers.

Additionality is a *condition* for effectiveness: a project can be extremely effective, but if the subsidy or loan is not needed to implement the project, then the instrument has not proven to be effective.

Additionality

The IOB evaluation of the LDC Fund defined additionality as the absence of market willingness to finance the project on reasonable conditions. The risks are too high in such cases *for the market*.

- Some indicators for additionality include:
- High political, financial or currency risks;
- There is barely any direct foreign investment in the sector;
- Commercial banks do not operate in the sector;
- It is difficult to find investors for the project;
- Involvement of other development banks; and
- The fund in question takes higher risks (for example, because of subordinated loans).

Catalytic impact

The *catalytic impact* is the ability of funds to generate other, often commercial resources with financing, such as subordinated loans.

Indicators for a catalytic impact include:

- There are no comparable projects with exclusively private investors;
- Other investors only participate after the fund has joined the project; and
- The fund takes higher risks.

Source: IOB

The fact that so much is known about the need for infrastructure and the great importance it has for socio-economic development is most probably a handicap. An evaluation can give the impression that it has to examine the 'evident'. The problem, however, is that in practice effectiveness is not so evident. According to the little research that there is on this issue, the impact on development (especially on poverty reduction) is less substantial than assumed. One reason is that investors focus insufficiently on the poorest groups and rely too much on automatic trickle-down effects. A second reason is that financing is not the only problem. Capacity problems on the receiving end are often an important reason why projects do not get off the ground in the first place. The third reason has been mentioned already: an effective project is not necessarily an effective programme. A project can be extremely successful, but if that project was going to take place anyway without (donor) financing, then the programme itself is ineffective (because it did not provide a service that would not have been otherwise provided).

The (old) evaluations of infrastructure projects (ORET) indicate that the long-term impact of subsidised export services, in the sense of strengthening trade relations and creating follow-up assignments, is limited. There is a real risk, however, that tied aid leads to high prices, which harms the efficiency and therefore the impact on development.

Financial sector development

There does not appear to be any clear synergy yet among insights from literature, the practice of programme development, systematic evaluation and feedback about results for policy makers. This also emerges from an analysis of evaluations of eight programmes in the area of financial service provision that the Netherlands has supported in recent years. Various evaluations had a review-like character, whereby consultants primarily examined the management structure and investigated the degree to which outputs were actually achieved. An element that complicated evaluation is that many programmes work through a local financial intermediary, for example a microcredit institution or a bank that focuses on small and medium enterprises. In such cases, there is trade-off between the demand for information, on the one hand, and an administrative burden for local banks, on the other hand. As a result, many evaluations get stuck at the level of the intermediary organisation. The evaluation then mainly assesses the functions of the intermediary, instead of the impact on the ultimate target group.

Another problem that various evaluations mention is the absence of clear results indicators when programmes are formulated. Development objectives are not clearly formulated in advance, which means monitoring cannot focus on them. As a result, in the end there is insufficient information for an evaluation to take place. Variables such as the number of businesses reached in the SME sector are of limited value as an indicator for measuring the effectiveness of a programme (IEG, 2013).[33]

With these qualifications in mind, we will nevertheless attempt to draw several conclusions from the evaluations that we have examined.

A first finding is that, too often, implementing organisations assume *additionality*. They should examine more critically how often resources were actually able to remove obstacles. One point that is related to additionality is the under-investment of programmes in the initial years. Teething problems are underestimated and spending pressure can lead people to be less critical in their considerations or choose to use the resources for other target groups.

Second, it appears that despite the obvious problem that poor households and comparable businesses do not have access to credit, in itself supporting local banks is inadequate. In practice, these resources only reach the target group to a limited degree. Furthermore, it appears from the scientific literature and the evaluations of microcredit that it is not so much the provision of untargeted credit to households that contributes to economic growth, but more so businesses' better access to credit. This means programmes need to focus more on microfinance. Providing credit to households (and micro-saving) can help the poorest households towards more sustainable consumption, but it is hardly the 'holy grail' that will drive economic activity.

In practice, access to credit is often not the only problem, and more attention needs to be paid to technical support, advisory services and the institutional context. One evaluation, for example, concludes that removing or mitigating exchange rate risks is only effective in countries with the right regulations and institutions. Another evaluation concludes – in line with literature about capacity building – that it is important not only to provide short-term support, but also to supervise customers longer. IEG mentions ownership as an important condition for the effectiveness of a programme.

Market development

The programmes and activities in the area of market development use different starting points. The programmes with the most funds focus mainly on promoting export and international or regional value chain development. The integration of markets is more of a focus for value chain programmes. There are also similarities: the same standard line of reasoning was behind many of these programmes, namely that more market knowledge and better market information must lead to better access to markets.

[33] In practice, the more thoroughly a programme is evaluated, the less positive the results are likely to be. Evaluations of microcredit are an example. This conclusion corresponds with the 'iron law' of Rossi (1987), which states that the better an evaluation's design is, the greater the chance that the researchers will not measure an impact. A reason for this is that consultants often focus too much on direct results and assume that the impact for the ultimate beneficiaries will happen regardless, thereby neglecting all the problems that occur in practice.

The various organisations have published important success stories. CBI mentions a reach of more than 500 export companies with an additional total turnover of EUR 228 million and 13,000 new jobs. Figures published by IDH[34] for individual projects suggest a reach of 700,000 farmers and an increase in productivity of 20%, and – in Kenya – crop yield improvements of 36% and price improvements of up to 75%. Evaluations of fair trade programmes note better use of credit opportunities, increased investment in schooling, better housing and stronger farmer organisations.

The evaluations are less clear when it comes to the (anticipated) net impact in the areas of increased productivity or higher sales. Good impact studies of the programmes are lacking.[35] Most evaluations remain strongly process- and output-oriented, but they say little about the anticipated impact, such as improved incomes and poverty reduction. When they do, it is not based on systematic research. To the extent that research has been conducted on specific target groups, it appears difficult to reach the poorest farmers.

Knowledge and skills

The ministry works with various instruments to strengthen the knowledge and skills of entrepreneurs in developing countries. The programmes' main hypothesis is that poor knowledge and skills stands in the way of economic growth and increased employment opportunities. This is essentially in line with what the literature has to say about bottlenecks in private sector development. A clear, coherent strategy is missing, however. The implicit assumption, which is also true for other PSD programmes, is that an integrated approach will rarely result in synergy. Various evaluations, however, mention the importance of the context and the interaction between bottlenecks for PSD. A lack of knowledge and expertise is rarely the only impediment – nor is access to finance for that matter.

The lack of coherence is partly the result of the development of individual programmes. Three of the four examined programmes are from the Dutch business sector and are run by the sponsors. In one case, it involves the direct interests of Dutch entrepreneurs. These programmes are generating support for development cooperation as they actively involve the Dutch business sector.

The question now is: what do we know about the effectiveness of these programmes? The evaluations do present estimates for individual projects, but sometimes confuse these with an assessment of the effectiveness of the overall programme. The question is not only whether a project was effective, but also whether the subsidy was a condition for its existence.

[34] IDH operates in more than 50 countries and works together with more than 300 businesses, NGOs, trade unions, financial institutions and government organisations in 18 sectors in order to make international commercial chains more sustainable.

[35] Several studies by LEI for IDH go the furthest in complying with the requirements of a good impact study.

The different evaluations paint a mixed picture. Some evaluations are positive about the impact, but they do not come up with particularly hard conclusions. This picture is in line with international findings. Although various studies argue that poor knowledge and skills are an obstacle for the growth of a business, little is known about the impact of interventions aimed at introducing improvements. Most evaluations – including international ones – do not accept hard conclusions. When they do, it appears that training can be effective in increasing entrepreneurs' financial literacy and management skills. Interventions that are goal-driven, focused and long term are more effective than short-term, less-focused projects. The ultimate impact, however, depends heavily on existing market conditions and the nature of the product. That may seem obvious, but it is not a given yet in the world of business development services.

Laws and regulations

This section focuses on several activities (financed by the Netherlands) that aim to improve the entrepreneurial climate in order to promote economic growth by means of legal and regulatory reforms. It concerns removing obstacles as well as developing an effective registration system of ownership rights, including land rights.

Several of the activities that were examined in this cluster focused on land reform. Encouraging private sector development was only one of the considerations in that respect, in addition to food security, the emancipation of communities and land conflict management. Dutch support was responsible for significant progress in determining land ownership titles in both Rwanda and Bolivia. A pilot project in the programme for registering land ownership titles in Rwanda revealed a positive impact in the form of higher investment and better access to land for women. The final impact of the land reform programme in Bolivia is unknown.[36]

The activities supported by the Netherlands in the laws and regulations cluster have considerably improved the formal conditions for setting up and running a business on paper. To what degree these projects also led to increased business activities cannot be determined based on the evaluations.

4.4 Coherence in the set of policy instruments

The large number of activities (more than 700) and implementing organisations raises the question of how the ministry can guarantee policy coherence. One conclusion from the description of the clusters in the previous chapter is that PSD rarely concerns isolated problems. It usually concerns a combination of bottlenecks, including poor physical infrastructure, insufficient availability of capital, limited access to market, and a shortage of knowledge and skills. The potential impact also depends on the degree of room for

36 With these types of programmes, it is important to separate the impact of land reform and the impact of land registration.

manoeuvre that individual businesses and sectors have in the entrepreneurial climate. Approaches that focus on a single problem are usually less effective.

The implementation of the Dutch PSD policy is characterised by a large number of separate specialised instruments, in which central implementing organisations operate with a high degree of independence. The ministry's level of engagement in managing the programmes was not high. The authorities responsible for PSD were handicapped by the limited availability of expertise on PSD. The coordinating role of the embassies is limited. Most embassies in partner countries did not have a PSD programme until recently either.

The ministry took a number of measures in the period 2007-2011 to address criticisms that PSD policy lacked coherence. This initially led to a greater exchange of knowledge with and among implementing organisations. Unfortunately, several initiatives petered out. By streamlining the list of countries in which the implementing organisations could operate, the ministry expected them to work more closely with one another and that the impact of the investments would increase. The organisations were reluctant, however, because they felt that this would harm demand.

Table 4 Distribution of central programmes; countries and regions (2005-2011)

	ORET	FMO	PSOM/PSI	CBI	PUM
Number of countries	40	76	57	59	81
50% of expenditures achieved with a number of countries	5	11	11	7	17
Percentage share largest country	26 %	9 %	7 %	15 %	8 %
Percentage share largest 15 countries	72 %	62 %	63 %	71 %	48 %
Percentage largest 25 countries	93 %	81 %	81 %	86 %	65 %
Percentage outside list of countries	31 %	20 %	16 %	20 %	20 %
Distribution (%) by continent:					
Europe and Central Asia	6 %	10 %	7 %	9 %	15 %
South Asia	12 %	23 %	10 %	24 %	13 %
East Asia and Pacific	15 %	8 %	24 %	13 %	21 %
Middle East and North Africa	3 %	1 %	6 %	5 %	7 %
Sub-Saharan Africa	60 %	41 %	39 %	21 %	27 %
Latin America and Caribbean	6 %	17 %	15 %	27 %	16 %

** For FMO it concerns three programmes: IDF, CD and MASSIF*
Source: figures from involved organisations; adapted by IOB.

An analysis of the distribution of expenditures in five extensive programmes in different countries and regions shows significant clustering for each instrument in a limited number of countries and regions, and an imbalanced distribution (table 4). This picture cannot be explained by income disparity between countries: the presence of instruments in the poorest countries is not greater than in countries with a higher income level. Other factors, therefore, play a role in allocation. In retrospect, we can conclude that restricting the country list to 15 or 20 countries would have had barely any impact on the distribution of resources, but that it would have considerably simplified coordination and synergy. This is barely the case today.

The risk of overlap is marginal; on the other hand, the lack of coordination does lead to a loss of efficiency and missed opportunities in terms of potential synergy. Studies (Triodos Facet, 2013a, 2013b, 2013d, 2013e) show that there was more synergy in the two countries in which embassies implemented a PSD programme (Ethiopia and Burundi) than in countries in which the embassies did not have an extensive PSD programme (Vietnam and Bangladesh). This finding emphasises the importance of coordination. The potential benefits of cooperation are being insufficiently exploited – at the expense of effectiveness. PSD is rarely about isolated problems, and yet that is precisely what the Dutch approach focuses on. Uncoordinated implementation can also cause further inefficiencies and the undesirable dissemination of scarce knowledge across several organisations. Closer cooperation between different instruments would enable implementing organisations to take better advantage of both general and country-specific knowledge. This is especially true for instruments that are somewhat comparable. In part, the above-mentioned risks are important because there is not much good insight on the development relevance and/or the results generated by the individual programmes.

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Annexes

Annex I International corporate social responsibility (ISCR) and public-private partnerships (PPPs)

International corporate social responsibility (ICSR)
The focus on international corporate social responsibility is not new. As early as the 1970s, various international organisations (including the UN, ILO, UNCTAD, WTO and OECD) were already establishing ICSR codes of conduct. Businesses should follow these guidelines so they can contribute to sustainable development, local capacity building, gainful employment, technology transfer and tax payments in host countries. Interest in ICSR has increased in recent years. The OECD's 2011 revised guidelines for multinational enterprises have extended ISCR norms to chain management, due diligence and human rights (the Ruggie Principles).

The Dutch government uses a variety of instruments across wide areas to promote corporate social responsibility in (Dutch) businesses in developing countries. The programmes/ interventions (IOB, 2013a) can be categorised as follows (in increasing order of government authority):

- Support for volunteer activities *(Endorsing)*;
- Communication and cooperation between various stakeholders *(Partnering)*;
- Active promotion of CSR *(Facilitating)*; and
- Enforcement of CSR results *(Mandating)*, by means of legislation, inspections, fines, procurement rules, trade policies, consumer guidelines and reporting requirements.

IOB research[37] shows that various internal and external factors influence the amount of attention businesses devote to international corporate social responsibility. External incentives that affect how businesses operate come from NGOs, research institutes, local governments and local communities. Businesses that operate internationally are sometimes put under pressure by NGOs.

Local governments and donors are seen as the main driving force behind ICSR and the establishment of ICSR frameworks. The role of governments is particularly important for supporting businesses in their efforts to implement ICSR. An active role for the public sector is also important when business and development objectives conflict. Most of the positive effects of public interference with ICSR are known as 'facilitating' and 'partnering' strategies, while 'mandating' and 'endorsing' have led to more mixed and sometimes even negative results.

[37] www.iob-evaluatie.nl/en/MVO

ICSR is mostly leveraged in the energy, mining, textile and small-scale production sectors, followed by agriculture. It is mainly larger businesses that report on ICSR. Empirical information on the impact of ICSR practices supported by donors in developing countries is scarce. An important reason for this is that it takes a certain amount of time before results are discernible. A systematic literature review of 45 studies conducted by IOB discovered that the impact of ICSR was strongest in individual businesses (39 studies), specific sectors (20) and local communities (21). Little is known about the impact at household level (7 studies). Only one study reported on the impact at the individual level. And 20 of 37 examined (valid) studies reported positive results; 8 were negative and 7 studies had mixed opinions. It is not always clear at all whether measured impacts can be traced back to government support. As a result, there is still no evidence of a clear connection between the government-backed interventions, the way in which businesses put ICSR into practice and its impact on (poverty in) developing countries.

Public-private partnerships (PPPs)

The ministry defines the PPP instrument as follows: 'A public-private partnership between government and the business sector (in many cases with the involvement of NGOs, trade unions and/or knowledge institutes), in which they agree to work together to achieve a common goal or carry out a specific task, and also agree to share the risks, responsibilities, resources, competencies and revenue' (Ministry of Foreign Affairs, 2010). This definition covers five main elements (IOB, 2013c):

1. Cooperation between the public and private sectors (sometimes also NGOs, social services partners and knowledge institutes) aimed at achieving a common (development) goal;
2. Clear agreement between the public and private parties about the objective of cooperation;
3. Combination of public and private financing;
4. Clear agreements between the public and private parties about the distribution of resources and the tasks; and
5. The spreading of risk between the public and private parties.

The reason why PPPs are used in development cooperation (DC) is to ensure the effectiveness of the design and increase the management and implementation of DC programmes and projects by pooling knowledge, capacities and resources. The partners work together to come up with joint solutions to problems. PPPs are expected to generate added value by:

- Contributing to policy making in the activity in question and ensuring that an issue gets on (and/or stays on) the international agenda;
- Contributing to quicker or more efficient policy implementation (such as laying drinking water pipelines or ensuring greater access to sustainable energy products);
- Making available additional private resources to achieve DC objectives, which would not have been available without the partnership;
- Introducing a new and more effective approach aligned with local conditions; preferably one that can be used in other places and on a larger scale; and

- Increasing support, which can also lead other partners to contribute to development objectives (Ministry of Foreign Affairs, 2010; World Bank Institute, 2010).

Research shows that there are six factors that give an indication of whether the use of PPPs will be successful and relevant:

1. Permanent involvement of the public partner. The government should not only provide the framework (such as safety and quality requirements), but also monitor and enforce it;
2. Clear legislation. This guarantees the private partner that there is protection of property, dispute settlement procedures and the enforcement of contracts for costs and revenue that are in proportion to the risks that are being taken;
3. Shared responsibilities. When a partnership is initiated, all parties must come to an agreement about the deployment of resources, the common objectives, communication procedures, the sharing of learned lessons and attention to cultural differences;
4. Partnership. It is important when choosing a partner to pay attention to the following factors: compatibility of each other's strengths, weaknesses and level of engagement, the ability of the partners to meet their obligations, the degree to which a partner can commit itself to the activity, and the way in which the partnership is led and how decisions are made;
5. Common vision and mutual trust. The position of one of the partners could change during the cooperation. For a business, this can occur as a result of situations in the market, such as price variations or a drop in demand. Mutual trust is needed to be able to cope with such situations, which put the partnership under pressure; and
6. Negotiating and determining the partners' various interests.

Each of these factors can affect the desired outcome, but the interaction between and the relative importance of each of these factors varies from case to case. Therefore, they are more of a practical tool and a checklist for collaborating partners than an outline or guarantee for success.

Annex II About IOB

Objectives

The remit of the Policy and Operations Evaluation Department (IOB) is to increase insight into the implementation and effects of Dutch foreign policy. IOB meets the need for the independent evaluation of policy and operations in all the policy fields of the Homogenous Budget for International Cooperation (HGIS). IOB also advises on the planning and implementation of evaluations that are the responsibility of policy departments of the Ministry of Foreign Affairs and embassies of the Kingdom of the Netherlands.

Its evaluations enable the Minister of Foreign Affairs and the Minister for Foreign Trade and Development Cooperation to account to parliament for policy and the allocation of resources. In addition, the evaluations aim to derive lessons for the future. To this end, efforts are made to incorporate the findings of evaluations of the Ministry of Foreign Affairs' policy cycle. Evaluation reports are used to provide targeted feedback, with a view to improving the formulation and implementation of policy. Insight into the outcomes of implemented policies allows policymakers to devise measures that are more effective and focused.

Organisation and quality assurance

IOB has a staff of experienced evaluators and its own budget. When carrying out evaluations it calls on assistance from external experts with specialised knowledge of the topic under investigation. To monitor the quality of its evaluations IOB sets up a reference group for each evaluation, which includes not only external experts but also interested parties from within the ministry and other stakeholders. In addition, an Advisory Panel of four independent experts provides feedback and advice on the usefulness and use made of evaluations. The panel's reports are made publicly available and also address topics requested by the ministry or selected by the panel.

Programming of evaluations

IOB consults with the policy departments to draw up a ministry-wide evaluation programme. This rolling multi-annual programme is adjusted annually and included in the Explanatory Memorandum to the ministry's budget. IOB bears final responsibility for the programming of evaluations in development cooperation and advises on the programming of foreign policy evaluations. The themes for evaluation are arrived at in response to requests from parliament and from the ministry, or are selected because they are issues of societal concern. IOB actively coordinates its evaluation programming with that of other donors and development organisations.

Approach and methodology

Initially IOB's activities took the form of separate project evaluations for the Minister for Development Cooperation. Since 1985, evaluations have become more comprehensive, covering sectors, themes and countries. Moreover, since then, IOB's reports have been submitted to parliament, thus entering the public domain. The review of foreign policy and a reorganisation of the Ministry of Foreign Affairs in 1996 resulted in IOB's remit being extended to cover the entire foreign policy of the Dutch government. In recent years it has extended its partnerships with similar departments in other countries, for instance through joint evaluations and evaluative activities undertaken under the auspices of the OECD-DAC Network on Development Evaluation.

IOB has continuously expanded its methodological repertoire. More emphasis is now given to robust impact evaluations implemented through an approach in which both quantitative and qualitative methods are applied. IOB also undertakes policy reviews as a type of evaluation. Finally, it conducts systematic reviews of available evaluative and research material relating to priority policy areas.

Evaluation and study reports of the Policy and Operations Evaluation Department (IOB) published 2009-2014

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Construction of a new bridge over the Zambezi river near Caia.

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Private sector development became an increasingly central focus of Dutch development policy, especially from 2010 onwards. Between 2005 and 2012, developing countries received a total of more than EUR 3.3 billion in support for private sector development. The international literature about bottlenecks in private sector development states the importance of a stimulating investment climate for the private sector. But what is known about the results of the Dutch policy? This policy review is looking into the results of the Dutch development policy on private sector development.

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